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IN THE

Supreme Court of the United States.

No. 559. October Term, 1936.

GENERAL BAKING COMPANY,

Petitioner,

v.

LUTHER A. HARR (SUCCESSOR TO WILLIAM D. GORDON), SECRETARY OF BANKING FOR THE COMMONWEALTH OF PENNSYLVANIA, IN POSSESSION OF THE BUSINESS AND PROPERTY OF THE FRANKLIN TRUST COMPANY, AND CHARLES I. ENGARD (SUCCESSOR TO JOHN J. SULLIVAN), SPECIAL DEPUTY IN CHARGE,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR APPELLEE.

I. COUNTER-STATEMENT OF THE CASE.

This case is here on bill and answer. Appellant seeks to establish a preference in a certain deposit account as the result of an agreement entered into between it and Franklin Trust Company (hereafter sometimes referred to as "Franklin") on August 25, 1925, as modified in August, 1930. The crux of the entire case is the effect to be given to this agreement. The agreement as set forth in appellant's bill is considerably qualified by appellee's answer

(R. p. 47-54) which answer makes specific reference to certain exhibits attached to the bill, consisting of letters written by appellant to Franklin Trust Company and by Franklin Trust Company to appellant, both prior and subsequent to the making of the oral agreement of August 25, 1925 (R. pp. 39-46). Appellant's statement of the case is confusing in that what are in reality the averments of its bill appear at first glance to be stated as established facts in the case, and appellant seems to base its argument upon the averments of its bill, without giving due consideration to the qualifications of the answer and the exhibits. Since the case comes up on bill and answer, the qualifications of the answer must be considered.

Appellant states that the terms and conditions of the agreement of August 25, 1925, were as follows:

> "(a) Petitioner would open a checking account with Franklin Trust Company and maintain therein an average balance of not less than $25,000.00 on which interest would be paid at the rate of 2 per cent. per annum; said account to be known as a 'Disbursement Account'.
>
> "(b) On Wednesday of each week, petitioner would forward from its New York office to Franklin Trust Company, a sum sufficient to maintain an average balance of not less than $25,000.00 in said checking account;
>
> "(c) Franklin Trust Company would accept from petitioner's distributor in Philadelphia, cash, also drafts and checks for collection, for the purpose of forwarding the cash, together with the proceeds of the drafts and checks, on Monday of each week to petitioner, or its depository, in New York City; said account to be known as a 'Deposit Account'.

"(d) Franklin Trust Company would select, subject to the approval of petitioner, certain correspondent banks in neighboring towns and cities in New Jersey, Delaware and Eastern Pennsylvania, to accept, from distributors of petitioner, cash, drafts and checks to be credited to, and subject to the check of Franklin Trust Company only, but earmarked as the funds of petitioner; a written acknowledgment of receipt of said cash, drafts and checks by each of said correspondent banks to be mailed immediately upon receipt of same to petitioner in New York City, and a credit advice to be sent immediately to Franklin Trust Company whereby all cash, drafts and checks accepted by said correspondent banks were to be credited to the said deposit account referred to in Clause (c) above, for the purpose of Franklin Trust Company forwarding the cash and the proceeds of the drafts and checks, together with the amount referred to in Clause (c) above, on Monday of each week, to petitioner, or its depository, in New York City.

"(e) Petitioner might, at the special request and for the sole benefit of Franklin Trust Company, from time to time, enter into separate and distinct oral agreements with Franklin Trust Company whereby petitioner would allow Franklin Trust Company to use certain sums from those accepted by it for the purposes set forth in Clauses (c) and (d) above, for certain periods of time, these sums to be called by petitioner's check only, instead of being forwarded by Franklin Trust Company. Under such agreements, and no other, would said fund, ever, become subject to check. (R. 31, 32.)"

Clauses (a) and (b) are admitted by appellee. Appellee's answer to (c) takes exception to the differentiation of the cash from the drafts and checks as set forth in appel-

lant's averment, and also qualifies the averment to the extent that it indicates that the cash, checks and drafts were accepted "for the purpose of" being forwarded to appellant in New York. Appellee's qualified averment of (c) reads as follows (R. p. 48):

> (c) "As by reference to the exhibits to the amended Bill of Complaint, as amended, will more specifically appear, your deponents aver that General Baking Company, the complainant, agreed to open a 'deposit account' in the Franklin Trust Company, wherein all moneys (including checks, cash and drafts) received by the three Philadelphia plants of the complainant were to be deposited, said deposits to be credited to the complainant, advices of each deposit to be forwarded to the offices of the General Baking Company in New York, and on Monday of each week the balance in the deposit account (as augmented by the funds received under the terms and conditions hereinafter set forth) to be forwarded by the Franklin Trust Company to the General Baking Company in New York or its depository."

In making this and further qualifications in its answer, appellee makes specific reference to the exhibits attached to appellee's bill. Because these exhibits indicate that there was no differentiation of checks and drafts from cash deposited but that they were all considered as "moneys" to go into the deposit account, and because they likewise indicate that a benefit was to accrue to Franklin Trust Company from these deposits, as well as a purpose of making funds available to appellant in New York, appellee has qualified this averment to the extent indicated. It should also be noted that the qualified answer does not admit that the drafts and checks were accepted "for collection." For

the same reasons, appellee's answer qualifies clause (d) as follows (R. p. 48):

> (d) "It was agreed by and between Franklin Trust Company and General Baking Company that Franklin Trust Company would make arrangements in certain towns in New Jersey, Delaware, Eastern Pennsylvania, and elsewhere, with banks of its selection, said banks to be approved by the complainant, to enable the cashiers of the distributors of the complainant in said towns to make deposits of their moneys (including cash, drafts, and checks) therein, said moneys to be credited in said banks to the account of the Franklin Trust Company, subject only to withdrawal by check of the Franklin Trust Company, a written acknowledgment of the receipt of said moneys to be mailed immediately upon receipt thereof by the outlying banks to the complainant, and a credit advice to be immediately forwarded to the Franklin Trust Company, all money so deposited in said outlying banks to be credited to the complainant's 'deposit account' in the Franklin Trust Company, and the proceeds thereof to be forwarded on Monday of each week to the General Baking Company or its depository in New York City."

It will be noted that the averment as qualified does not state that the cash, drafts and checks deposited in the correspondent banks were "earmarked as the funds of petitioner".

Clause (e) of the averment is qualified to the extent that it recites that the agreements to permit Franklin Trust Company to use certain funds were for the sole benefit of Franklin Trust Company. Clause (e) as qualified by appellee reads as follows (R. p. 49):

> (e) "Defendants have no knowledge that the agreement as therein set forth was entered into by

the complainant and the Franklin Trust Company for the sole benefit of the Franklin Trust Company, and if the same is material, demand proof thereof. Defendants aver, moreover, that the allegation that said contract was entered into for the sole benefit of the Franklin Trust Company is a conclusion of law and therefore irrelevant.

"Defendants aver, moreover, that under the terms and conditions of the agreement entered into between the Franklin Trust Company and the General Baking Company, as set forth in the amended Bill of Complaint, as amended, and as qualified by this Answer, the Franklin Trust Company was authorized by the General Baking Company to retain and use all sums of money deposited by the General Baking Company in the Franklin Trust Company or the outlying banks, including not only the funds deposited in accordance with the special arrangements as set forth in subdivision E of paragraph 8 of the amended Bill of Complaint, as amended, and as qualified in this Answer, but also all other funds deposited in said 'deposit account' and in the outlying banks, in accordance with the agreement of the parties as set forth in subdivisions C and D of the amended Bill of Complaint, as amended, and as qualified in this Answer, for those periods of time during which said funds were in the possession of Franklin Trust Company and/or the outlying banks, and that there was thus created the relationship of depositor and depository with all the rights and responsibilities implicit therein."

On page 7 of its brief appellant's statement of the case recites that:

"On Friday, October 2, 1931, there were delivered to Franklin Trust Company for collection, checks and drafts totalling $1,005.52, and on Saturday, October 3, 1931, checks and drafts totalling $8,747.66."

For reasons already set forth, the use here of the phrase "for collection" should be eliminated as not warranted by the averments of the bill as qualified by the answer.

On page 7 of appellant's statement of the case there appears the following:

> "On the same dates there was delivered to Franklin Trust Company cash totalling $40,642.67. This cash was likewise to be forwarded to petitioner's depository in New York City in accordance with the provisions of Clause (c). (R. 37.)"

Appellee objects to the use of the phrase "this cash". The whole question in this case is whether Franklin Trust Company was to have the use of the funds of General Baking Company and furnish its own funds at the required times, or whether it was to segregate from its funds the actual deposits made by appellant and transfer these segregated deposits to New York. It is important to note that the statement of appellant that "this cash" was to be sent to New York,—the very point in dispute,—is not justified by the averments of the bill as qualified by the answer.

On Page 8 of its brief, appellant states that the proceeds of checks deposited with Franklin Trust Company on October 3, 1931, "together with the $40,842.51 in cash, were diverted to and mingled with the cash funds of Franklin Trust Company without petitioner's consent or approval (R. 38)". This statement is based on Paragraph 24 of the amended bill of complaint as amended, and this paragraph is qualified by the corresponding paragraph of appellee's answer to read that the funds "were mingled with the cash funds of Franklin Trust Company without first obtaining complainant's *specific* consent or approval therefor" (R. 52). (Italics supplied.)

On Page 9 of its brief, appellant states that:

"The Amended Bill of Complaint as Amended concludes with a prayer (1) that the court declare petitioner to be the owner of the $32,403.26, and (2) that the court declare the $49,590.17 to be impressed with a trust in petitioner's favor (R. 38, 39)."

As a matter of fact the prayer of the bill went much further, and appellee feels that since a jurisdictional question is involved, the entire prayer should be set forth. It reads as follows (R. 38, 39):

"Wherefore, your orator prays:

"(a) That it be ordered and decreed that the defendants hold in trust for your orator the sum of $49,590.17, accepted by the Franklin Trust Company for the purpose of forwarding to your orator in New York City;

"(b) That it be ordered and decreed that the total sum of $32,403.26, collected by the correspondent banks for forwarding by the Franklin Trust Company to your orator in New York City, and now held in escrow, is the property of, and belongs to, your orator;

"(c) That it be ordered and decreed that your orator has a lien on the assets of the Franklin Trust Company now in the possession and control of the defendants;

"(d) That it be ordered and decreed that your orator has a lien on the sum of $32,403.26, now held in escrow;

"(e) That it be ordered and decreed that the defendants pay immediately to your orator the said sum of $49,590.17, with legal interest thereon from October 5, 1931;

"(f) That it be ordered and decreed that the sum of $32,403.26, together with interest thereon, now held in escrow be immediately paid to your orator;

"(g) That such other and further relief as the equities in this case may require and as your Honors may deem proper be ordered and decreed."

With the foregoing qualifications, appellee is in accord with appellant's statement of the case.

II. ARGUMENT.

Summary.

Appellee contends that the Circuit Court of Appeals for the Third Circuit properly ruled that appellant's bill in equity seeking to establish a preference in the assets of the closed Franklin Trust Company, a banking institution of the Commonwealth of Pennsylvania, should be dismissed by the District Court. Appellee's argument in support of the ruling of the Circuit Court of Appeals may be summarized as follows:

1. Although jurisdiction to entertain appellant's bill in equity existed under the diversity of citizenship clause, the District Court should have refused to entertain jurisdiction because—

(a) Entertaining jurisdiction constituted an interference with the administration by the Commonwealth of Pennsylvania through its executive and judicial departments of the liquidation of a closed banking institution—a quasi public corporation subject to regulation under the laws of the State;

(b) Appellee, as Secretary of Banking of the Commonwealth of Pennsylvania, and Receiver of the Franklin Trust Company, is, under the decisions of the Supreme Court of Pennsylvania, a mere stakeholder, and consequently, the real respondents—the other claimants to the assets of the Franklin Trust Company—are indispensable parties to this litigation, and the failure of appellant to join them in its bill is fatal to its suit.

(c) Appellant's bill seeks to obtain possession and control of a portion of the res being administered by the

state officers, subject to the supervision and control of the state court, and consequently is a proceeding quasi in rem, as to which the District Court should not entertain jurisdiction.

2. If the merits are to be considered, the dismissal of appellant's bill was nevertheless proper, as held by the District Court, and the Circuit Court of Appeals in its original opinion because—

(a) All deposits as to which appellant sought a preference, both of checks and cash, made in the Franklin Trust Company and in correspondent banks of the Franklin Trust Company, gave rise immediately upon deposit to a debtor-creditor relationship between the Franklin Trust Company and appellant. Accordingly appellant is entitled only to the status of a depositor;

(b) No preference as to the checks and drafts still in the possession of the Franklin Trust Company at the time of its closing exists by reason of the Pennsylvania Bank Collection Act of June 13, 1931, P. L. 568, because by that act a bank of deposit is an agent of the depositor for collection only "in the absence of an agreement to the contrary", and in this case such an agreement to the contrary existed.

I. The Federal Courts Should Not Exercise Jurisdiction Over This Controversy.

Appellee admits that the District Court had jurisdiction to entertain appellant's Bill in Equity, since diversity of citizenship existed and the amount in controversy exceeds $3000., exclusive of interest and costs. As was said, however, in *United States v. Bank of New York & Trust Company*, 296 U. S. 463, 480, 80 L. Ed. 331, 340 (1936):

> "The statutory grant of jurisdiction to the District Court leaves open the question of the propriety of its exercise in particular circumstances. Even where the District Court has acquired jurisdiction prior to the State proceedings, the character and adequacy of the latter proceedings, in relation to the administration of assets within the State and the status of those assets, may require, in the proper exercise of the discretion of the Federal Court, that jurisdiction should be relinquished in favor of the State administration."

In that case, as in the case at bar, the question involved was whether a Federal Court should entertain jurisdiction over a proceeding intended to remove from the custody and control of a statutory liquidator, acting under the protection of a State Court, assets which were being liquidated for the benefit of creditors of an insolvent institution. It remains accordingly to determine whether or not jurisdiction should be exercised.

(a) *The Federal Courts should not interfere with the comprehensive scheme of distribution of the assets of a banking institution of the State provided by the State statute.*

This Court has decided in *Pennsylvania v. Williams*, 294 U. S. 176, 79 L. Ed. 481 (1934); *Gordon v. Ominsky*, 294 U. S. 186, 79 L. Ed. 848 (1934); and *Gordon v. Washington*, 295 U. S. 30, 79 L. Ed. 1282 (1934), that the Secretary of Banking of the Commonwealth of Pennsylvania is entitled to proceed with the orderly liquidation of a banking institution, or building and loan association, of which he has taken possession pursuant to the Banking Act of 1923, P. L. 807, 7 P. S. 1-ff., as amended, without interference from the Federal Courts through the appointment of federal re-

ceivers applied for on bills of equity asserting diversity of citizenship as the basis for jurisdiction. In *Pennsylvania v. Williams, supra,* the Court said:

> "The relief sought, an injunction and the appointment of receivers, was aimed at the prevention of irreparable injury, from the waste of the assets of the insolvent corporation which would ensue from a race of creditors to secure payment of their claims by forced sale of the corporate property. By local statutes elaborate provision is made for accomplishing the same end, through the action of a state officer, in substantially the same manner and without substantially different results from those to be attained in receivership proceedings in the federal courts. There is no allegation or contention that the procedure thus provided is inadequate, or that it will not be diligently and honestly followed. In such circumstances the discretion of the district court, invoked by the petition of the commonwealth, should have been exercised to relinquish the jurisdiction in favor of the statutory administration of the corporate assets by the state officer.
>
> The question is not the ordinary one of comity between a federal and a state court, each asserting jurisdiction over the same subject matter, and the same property, and where there are shown no special reasons addressed to the discretion of the court first acquiring jurisdiction for relinquishing its jurisdiction in favor of the other. Compare McClellan v. Carland, 217 U. S. 268, 281, 282, 54 L. Ed. 762, 767, 30 S. Ct. 501; Hyde v. Stone, 20 How. 170, 175, 15 L. Ed. 874, 875; Chicot County v. Sherwood, 148 U. S. 529, 534, 37 L. Ed. 546, 548, 13 S. Ct. 695; Re Chetwood, 165 U. S. 443, 460, 41 L. Ed. 782, 788, 17 S. Ct. 385; with Harkin v. Brundage, 276 U. S. 36, 72 L. Ed. 457, 48 S. Ct. 268, supra; Rogers v. Guaranty Trust Co., 288 U. S. 123, 77 L. Ed. 652, 53 S. Ct. 295, 89 A. L. R. 720; Kansas City Pipe Line Co. v. Fidelity Title & T. Co. (C. C. A. 8th) 217

F. 187; First Nat. Bank v. Horuff (C. C. A. 5th) 65 F. (2d) 319. Here no state court is asserting jurisdiction, but the state officer, charged by the statutes of the state with the duty of supervising its own building and loan associations and of liquidating them by an adequate procedure when insolvent, asks to proceed with the liquidation. See Amos v. Trust Co. of Florida (C. C. A. 5th) 54 F. (2d) 286, 288.

A court of equity, which in its discretion may refuse to protect private rights when the exercise of its jurisdiction would be prejudicial to the public interest, see United States ex rel. Greathouse v. Dern, 289 U. S. 352, 359, 360, 77 L. Ed. 1250, 1254, 1255, 53 S. Ct. 614, or deny relief upon performance of a condition which will safeguard the public interest and secure substantial justice to the complainant, see Harrisonville v. W. S. Dickey Clay Mfg. Co., 289 U. S. 334, 338, 77 L. Ed. 1208, 1211, 53 S. Ct. 602, would seem bound to stay its hand in the public interest where it reasonably appears that the private right will not suffer. It is in the public interest that federal courts of equity should exercise their discretionary power with proper regard for the rightful independence of state governments in carrying out their domestic policy. Fenner v. Boykin, 271 U. S. 240, 243, 244, 70 L. Ed. 927, 928, 46 S. Ct. 492; Massachusetts State Grange v. Benton, 272 U. S. 525, 527, 71 L. Ed. 387, 390, 47 S. Ct. 189; Matthews v. Rodgers, 284 U. S. 521, 525, 76 L. Ed. 447, 451, 52 S. Ct. 217; cf. Central Kentucky Natural Gas Co. v. Railroad Commission, 290 U. S. 264, 273, 78 L. Ed. 307, 313, 54 S. Ct. 154. It has long been accepted practice for the federal courts to relinquish their jurisdiction in favor of the state courts, where its exercise would involve control of or interference with the internal affairs of a domestic corporation of the state. See Rogers v. Guaranty Trust Co. supra (288 U. S. 130, 131, 77 L. Ed. 656, 657, 53 S. Ct. 295, 89 A. L. R. 720). Compare Burnrite

Coal Briquette Co. v. Riggs, supra (274 U. S. 212, 213, 71 L. Ed. 1005, 1006, 47 S. Ct. 578); Canada Malting Co. v. Paterson Steamships, 285 U. S. 413, 419-423, 76 L. Ed. 837, 840-842, 52 S. Ct. 413; Langnes v. Green, 282 U. S. 531, 541, 75 L. Ed. 520, 526, 51 S. Ct. 243. There are stronger reasons for adopting a like practice where the exercise of jurisdiction involves an unnecessary interference by injunction with the lawful action of state officers. Matthews v. Rodgers, supra (284 U. S. 525, 76 L. Ed. 451, 52 S. Ct. 217)."

The same statute, the Banking Act of 1923, P. L. 809, as amended by the Act of May 5th, 1927, P. L. 762, 7 P. S. § 1-ff. involved in the *Williams* case is before the Court here. It provides for the regulation and supervision of financial institutions, including banking and building and loan associations. Section 21 authorizes the Secretary to take possession of the business and property of a banking institution if its condition is "unsafe or unsound", or if the institution has violated the law or an order of the Secretary; he can take possession only after notice and hearing and after securing the approval of the Attorney General. Section 22 requires the Secretary to file a certificate in his office and in that of the prothonotary of the court having jurisdiction (by Section 19 the Court of Common Pleas of Dauphin County or of the county in which the corporation is located), stating that he has taken possession of the business and property of the institution. The association may, under Section 23, obtain court review of the action by application within ten days for a show cause rule. The Secretary, after giving notice to all persons holding assets of the institution (Section 25), and after taking an inventory of the assets (Section 26), may either suspend or continue the business pending determination

of whether or not to liquidate the affairs of the institution (Section 27). By Section 28 the Secretary is authorized to surrender possession upon the resumption of business by the institution or the sale of its assets to a successor or independent corporation. Section 29 gives the Secretary "except as herein otherwise provided", the status and powers of a receiver of a court of equity. The court having jurisdiction is given, by Section 30, power to enforce orders to enable the Secretary to perform his duties under the Act. Under Section 31 his possession continues until liquidation, resumption of business by the institution, surrender under Section 28, the substitution of liquidating trustees elected by shareholders or appointed by the court as provided in Section 50, or payment of the creditors in full. The Secretary is authorized, with leave of court, to compromise claims (Section 34) and to prosecute or defend suits pending at the time he takes possession, and to sue to recover assets to which the institution has a claim (Section 35). During his possession, no lien shall attach or execution issue against the property of the institution, and no pledgee shall, without permission of the Secretary or order of the court, sell the collateral or pledge (Section 36). Before liquidation, the Secretary must give notice to creditors and depositors (Section 41) and have an inventory and appraisement made by disinterested persons and filed with the prothonotary of the court (Section 38). No claims other than those of depositors shown to be such on the books of the institution, or beneficiaries of or claimants against trust estates, shall be allowed unless the claimant files with the Secretary within four months from the date of notice of taking possession a sworn statement of claim (Section 42). By Section 45 the Secretary must file in court a final or partial account of claims allowed or

rejected, and any party in interest may file objections in the court either to the disallowance of his own claim or the allowance of the claims of others; if no account is submitted within one year, a court order directing its submission may be obtained. Section 46 provides that the account is binding and conclusive, except as to those parts to which objection has been made in court, and directs distribution in accordance therewith. If the account were partial, its confirmation is not conclusive on claims specified in subsequent accounts (Section 47). The court is to hear and determine matters in controversy (Section 48). Expenses of administration are to be paid out of the institution's funds and are subject to the approval of the court (Section 49). Section 50 provides for the election of liquidating trustees by the shareholders, or appointment by the court in default of election, if a balance remains after the final account has been filed and the creditors paid in full.

The decision in *Pennsylvania v. Williams, supra,* establishes that this statute adequately protects the interest of creditors of corporations being liquidated by the Secretary of Banking. The question in the instant case is whether the doctrine enunciated in the Williams case should be followed to its logical conclusion, in order that the Secretary of Banking may complete an orderly liquidation in the state court without being forced to defend actions in the federal courts seeking to dispossess him of part of the assets under his control, brought by persons who are unwilling to file their claims in the manner provided by the State Act.

To require the Secretary of Banking to defend such suits complicates the otherwise simple scheme of distribution provided by the statute. It means that claims can be filed and proved in two places,—first, with the Secretary,

pursuant to the State Act; second, with the federal court. The Secretary is thereby prevented from liquidating the assets entirely in the manner prescribed by the State statute and forced to engage in extended litigation in a different tribunal. Distribution of the assets through the process provided by the State statute is either delayed thereby, or else the claims brought in the federal court are ignored and distribution is completed before the Federal litigation is terminated. Compare *Richle v. Margolies*, 279 U. S. 218, 224 (1929), where the Court said:

> "The power to fix the time for distribution may include the power, in the exercise of judicial discretion, to decline to postpone distribution awaiting disposition of litigation in another court over a contested claim."

Such a result would, of course, be most inequitable and merely gives point to the argument that all questions respecting distribution of the assets in the possession of the Secretary should be determined under the direction and control of the state court, in accordance with the State Act. On no other basis can the principle established in the Williams case be carried into effect as a practical matter.

It should be emphasized that the status of a State officer in liquidating a quasi public corporation, pursuant to a statutory scheme of distribution prescribed by State law, is quite different from that of private litigants who attempt to evade the jurisdiction of the federal courts, in cases where diversity of citizenship is involved, on the plea that an adequate and exclusive remedy is provided in a state tribunal. A State statute cannot, of course, restrict federal jurisdiction, but where such a statute outlines a comprehensive State policy for dealing with the affairs of a semi-public State corporation, federal courts of equity, in

the exercise of their discretionary powers, should decline to take action which cannot fail to hinder, impede, and delay the procedure set up by the State for dealing with semi-public corporations of its own creation.

As pointed out by Justice Stone in *Pennsylvania v. Williams, supra,* such is the rule where interference with the internal affairs of a domestic corporation of the State is concerned. See *Rogers v. Guaranty Trust Co.,* 288 U. S. 130. And there are stronger reasons for adopting a like practice where the State has prescribed a complete system of distribution of the assets of its own banking institutions by one of its own officers.

Since it has been determined in *Pennsylvania v. Williams, supra,* and the other cases referred to above, that the Secretary of Banking, as opposed to federal receivers, should liquidate the assets in question, he should be given all of the rights and privileges which would inure to the benefit of a technical receiver of the State Court. Among the most important of these benefits is the right to have determined in the Court of the receivership all questions affecting title or prior claim to the assets being liquidated.

In determining whether State Banking Commissioners liquidating insolvent State institutions were subject to suit in federal courts, the district courts and the circuit courts of appeals have been inclined to base their conclusion upon whether or not the state statute made the commissioner a receiver of the state court. It is submitted that this distinction is a sterile one. The real test should be whether the proposed suit interferes with the orderly administration of the assets of the institution in question under the control of the commissioner or secretary. If it does, the federal court should not entertain jurisdiction.

In the instant case, as pointed out above, the attempt is to deprive the Secretary of a portion of the assets under his control, and this without permitting the other interested parties, *i. e.*, depositors and creditors of the bank, to be heard. Such a proceeding cannot fail to interfere with the orderly administration of the estate.

(b) *The Federal Courts should refuse to entertain jurisdiction of the present controversy because indispensable parties are not before the Federal Court.*

If the Secretary is required to defend suits brought against him in the federal courts, he is converted from a mere stakeholder into a party litigant in violation of the scheme of liquidation prescribed by the State statute. In *Franklin Trust Company of Philadelphia Case*, 319 Pa. 193 (1935), the Supreme Court of Pennsylvania, following earlier decisions, refused to permit the Secretary of Banking to appeal from a decree of the court of Common Pleas No. 5 of Philadelphia County in which he had filed his first accounting of the assets involved in the case at bar. The decree in question established a preferred claim to certain of the assets held by the Secretary as Receiver. The Court said:

> "The appeal of the Secretary of Banking . . . is, upon the motion of the appellee, quashed. We find from the agreed stipulation of the facts that he has neither an equity nor a legal interest, other than that of a mere stakeholder, in the decree from which this appeal is taken, and so he has no standing to appeal; Cameron v. City Bank of New York, 284 Pa. 187, 130 A. 407; Cameron v. Carnegie Trust Co., 292 Pa. 114, 117, 140 A. 768."

Because the statutory liquidator (in that case, the Superintendent of Insurance of the State of New York)

was only a stakeholder, this Court, in *United States v. Bank of New York & Trust Co.*, 296 U. S. 463, held that the federal courts should decline to entertain jurisdiction over a claim to the assets in the hands of the liquidator unless and until all other parties claiming such assets had been joined as parties, saying (p. 480):

> "In the instant cases, not only had the state court first acquired jurisdiction, but there are numerous persons whose claims in relation to these funds are in course of adjudication. Whether or not their claims are valid against the claim of ownership by the United States, they are entitled to be heard and they are indispensable parties to any proceeding for the disposition of the property involved. *They have not been made parties to the present suits, and this fact in itself would be a sufficient reason for the District Court to refuse to proceed in their absence.* Only the stakeholders are defendants. The adverse claimants are parties to the respective proceedings in the state court, and from every point of view the principles governing the convenient and orderly administration of justice require that the jurisdiction of the state court should be respected." (Italics supplied.)

So, in the instant case, the depositors and other creditors of the Franklin Trust Company are entitled to be heard in the state court. They are powerless to assert their interests in the federal court. The Supreme court of the State has ruled that the Secretary of Banking is only a stakeholder. Yet, in the present proceedings, he is forced to undergo the expense of extensive litigation in the federal courts in order to prevent a substantial portion of the assets in his control from being removed from his possession. It is submitted that the Federal Courts should refuse to entertain jurisdiction of appellant's bill and re-

quire it to file its claim in the State Court where all interested parties can appear of record.

(c) *Appellant's bill seeks to obtain possession and control of a portion of the res being administered by the Secretary of Banking under the supervision and control of the State Court; it is, accordingly, a proceeding quasi in rem, of which the Federal Court should not entertain jurisdiction.*

It should be noted that, despite the contention of the appellant to the contrary, the present proceedings were not instituted merely to liquidate a claim. The prayer of the amended Bill (R. pp. 38-39) is that it be ordered and decreed that certain of the assets in the possession of the Secretary of Banking are held in trust for the appellant, that the appellant has a lien on such assets, and that the appellee shall pay immediately to the appellant the sums of money as to which it is asserted a trust arises.

It matters not whether the present proceeding is strictly in rem. The vital point is that the appellant attempts to withdraw from the possession and control of the Secretary of Banking, as supervised by the State Court, a portion of the res which he is in the process of administering. The bill for an accounting as filed in *United States v. Bank of New York & Trust Co., supra,* was not *per se* an action in rem. Yet, this Court held (296 U. S. 477) that, since the proceedings in the state court were quasi in rem, and since control of the funds was essential to the exercise of that Court's jurisdiction to protect the rights of the claimants, the Federal Courts should decline to entertain jurisdiction of the bill. The Court stated (p. 477):

> "The principle, applicable to both federal and state courts, that the court first assuming jurisdiction

over property may maintain and exercise that jurisdiction to the exclusion of the other, is not restricted to cases where property has actually been seized under judicial process before a second suit is instituted. It applies as well where suits are brought to marshal assets, administer trusts, or liquidate estates, and in suits of a similar nature, where, to give effect to its jurisdiction, the court must control the property. Farmers Loan & T. Co. v. Lake St. Elev. R. Co., 177 U. S. 51, 61, 44 L. Ed. 667-671, 20 S. Ct. 564. If the two suits are in rem, or quasi in rem, so that the court must have possession or control of the res in order to proceed with the cause and to grant the relief sought, the jurisdiction of one court must, of necessity, yield to that of the other. Penn General Casualty Co. v. Pennsylvania, 294 U. S. 189-195, 79 L. Ed. 850-55, 55 S. Ct. 386. This principle is applied in the discharge of the long recognized duty of this court to give effect to such 'methods of procedure as shall serve to conciliate the distinct and independent tribunals of the states and of the union so that they may cooperate as harmonious members of a judicial system coextensive with the United States' " (citing cases).

In that case, as here, it was urged that the suit in the federal court was not in rem but in personam, and that to allow the federal court to pass upon the right asserted would not necessarily interfere with the jurisdiction or control of the state court—or here, the Secretary of Banking acting under the control of the state court—over the res. This Court held, however, that the suits were not merely to establish a debt, or a right to share in property, but included a demand that the depositaries accounting pay over to the complainant, as the sole and exclusive owner, the entire funds in their hands. In that case the entire funds were sought. Here, only a portion of the assets is claimed. The

principle, however, is identical. The object of the suits is to take property from the Secretary of Banking, where it is under the control of the state court, and to vest it in the complainant to the exclusion of all those whose claims are being adjudicated in the state proceedings.

Vacuum Oil Co. v. Land Title Guaranty & Trust Co., 80 F. (2d) 476 (C. C. A. 6th, 1935) decided prior to the decision of this Court in *United States v. Bank of New York & Trust Co*, *supra*, held that the federal court could properly entertain jurisdiction of a bill in equity against the Ohio State Superintendent of Banks asking for an accounting and a payment over to the plaintiff of the sum of $35,000. deposited with a closed bank being liquidated by the Superintendent, under an escrow agreement which it was claimed created a trust fund of the sum involved. The case quite clearly conflicts with the later decision of this Court in the *New York Bank & Trust Company* case which, as noted above, was also a bill for an accounting. Accordingly, it must be deemed to have been overruled by that case and, consequently, to have no bearing on the case at bar. The basis of the decision was that the bill for an accounting was essentially an action in personam but, as pointed out in the *New York Bank & Trust Company* case, the effect of the prayer of the bill is to remove from the possession and control of the statutory liquidator a part of the res in the process of liquidation. Accordingly, the action is quasi in rem and jurisdiction will not be entertained by the federal courts.

It may be suggested that the Secretary of Banking is not a receiver of the state court and that, accordingly, he is not entitled to the protection afforded to a court officer. Cases can be referred to where state banking commissioners, under statutes somewhat different from that of Pennsylvania, have been required to submit to suit in the federal courts where the object sought was to establish

claims and priorities to the assets being liquidated and distributed. Compare *Allen v. United States*, 285 Fed. 678 (C. C. A. 1st, 1923); *MacDonald v. Guy*, 63 Fed. (2d) 334 (C. C. A. 1st, 1933); *Amos, Comptroller of State of Florida v. Trust Co. of Florida*, 54 Fed. (2d) 286 (C. C. A. 5th, 1931); *Interstate Trust & Banking Co., et al., v. Jones County (Miss.)*, 77 F. (2d) 806 (C. C. A. 5th, 1935). In these cases, however, the statutes of the particular states in question had either been construed by the highest court of the state so as to make the Commissioner subject to suit in any court of appropriate jurisdiction, or were so interpreted by the federal court in which the issue was raised. The Pennsylvania Act in Section 29 (1923 P. L. 809) 7 P. S. 29, as pointed out above, provides:

> "Except as herein otherwise provided, the Secretary shall, when he has taken possession of the business and property of a corporation or person, have all the rights, powers and duties of a receiver appointed by any court of equity in this Commonwealth;"

Moreover, the entire process of liquidation is subject to the control of the state court as appears from the summary of the statute on pages 15-17 of this brief.*

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*Although passed after the present suit was instituted, the provisions of the Department of Banking Code of May 15, 1933, P. L. 565, 71 U. S. 733, are important as showing the present law of Pennsylvania respecting the status of the Secretary of Banking when he takes possession of a banking institution for purposes of liquidation. Article VI, Section 601, of the Code provides:

> "Whenever the (Banking) Department takes possession of the business and property of an (banking) institution, the Secretary shall, by operation of law, simultaneously take over such possession from the Department and become Receiver of such institution subject to the provisions of this Act. His official title, when thus in possession of the business and property of an institution, shall be Receiver of such institution."

Whether or not the Secretary by this provision becomes technically a receiver of the Court of Common Pleas,

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Section 701 of Article VII of the Code provides:

"Except as otherwise provided in this Act, the Secretary, when he has taken possession of the business and property of an institution, shall be responsible to the Court in which the certificate of possession is filed and not to any other Court. His rights, powers and duties shall be those of a general Receiver appointed by any Court of Equity in this Commonwealth, except as such rights, powers and duties are increased or limited by the provisions of this Act."

Section 709 of Article VII of the Code provides:

"The Court in which the certificate of possession is filed shall sit as a Court of Equity. It shall have the power, upon petition of the Secretary, to make and enforce any appropriate order to enable him, with the utmost dispatch, to discharge his duties in connection with the business and property of any institution of which he has taken possession, as Receiver, pursuant to the provisions of this Act."

Sub-section B of Section 713 of Article VII of the Code provides:

"B. All claims against the institution, suit upon which has not been commenced prior to the time the Secretary took possession, shall be presented in the regular manner provided by this Act for presentation of claims. Neither a depositor or other creditor of the institution, nor any other claimant, may maintain any action at law or in equity upon such claim, except by regular method provided by this Act for exceptions to the accounting of the Secretary as Receiver. . . ."

Sub-section C of Section 713 of Article VII provides:

"C. Any action at law or in equity, based upon a cause of action against the institution of which the Secretary is Receiver, which may be brought against the Secretary as Receiver, shall be instituted only in the Court in which the certificate of possession is filed."

The above Act makes clear the policy of the State to give to the liquidation of an insolvent banking institution the status of a receivership in the State Court. That policy this Court stated in *Pennsylvania v. Williams, supra,* should be respected by Federal Courts of Equity in exercising their discretionary power. It is, of course, true, as suggested in appellant's brief (pp. 19-22), that a state statute cannot limit the jurisdiction of the federal courts. The question here, however, is not whether the District Court had jurisdiction of appellant's bill, but whether, in the exercise of its equitable discretion, it should have refused to hear the controversy and relegated the appellant to his rights in the state court.

in which his certificate of taking possession has been filed, is immaterial. As a practical matter, he is to all intents and purposes the arm of that Court. To it he must account. With it are filed all exceptions to his account. By it are determined all questions relating to priorities and claims to the assets being administered. Surely, it is ignoring the substance of the situation to contend that the state court does not have complete jurisdiction over the disposition of the res consisting of the assets being administered. And, if that court has such jurisdiction, this Court has ruled that the state court alone should pass on all attempts to remove those assets from the possession of the statutory liquidator.

In *United States v. Bank of New York & Trust Co., supra*, the Court said (p. 475):

> "When the state court directed the Superintendent of Insurance to take possession of the assets of the United States branches, and to conserve those assets until its further order, the court took jurisdiction of the res. While the Superintendent was a statutory liquidator, he took possession under the direction of the court and the fund was at all times subject to the court's control."

It was concluded that the control of the state court should not be interfered with through the entertaining by the federal court of the complainant's bill for an accounting.

To the same effect is *Reconstruction Finance Corporation v. Zimmerman*, 76 F. (2d) 313 (C. C. A. 4th, 1935). In that case the Reconstruction Finance Corporation sought an injunction from the Federal District Court for the Eastern District of South Carolina restraining the Conservator of a South Carolina State Bank, in process of liquidation, from paying dividends to depositors before paying off a

loan made by the Reconstruction Finance Corporation. The Conservator had qualified as a Receiver pursuant to a State statute which directed him to conduct the litigation under the supervision of the state court (Act of May 16, 1933, 38 Statutes at Large, 489). He was not, however, appointed receiver by the state court. The Court said:

> "There can be no question that defendants, under the direction of the State Court, were acting as receivers just as much so as if they had been appointed by the Court. The State Court was directing all matters connected with the liquidation and, through the defendants, had such possession of the res as would remove them from the jurisdiction of all other courts."

The plaintiff's bill was dismissed for want of jurisdiction.

People's Trust Company v. United States, 23 F. (2d) 381 (C. C. A. 1st, 1928), illustrates the same argument. There, the State Banking Commissioner of New Hampshire, acting under Chapter 68 of the Laws of the State of New Hampshire of 1911 (which nowhere refers to the Commissioner as a court receiver), upon petition to the state court (which petition the State Act gave the state court no discretion to deny) took possession of an insolvent state bank. The United States filed with the Commissioner a claim for priority for deposits made by postmasters. Thereafter, it brought a bill against the Banking Commissioner in the federal court to establish its claim. The Circuit Court of Appeals for the First Circuit held that the federal court should not entertain jurisdiction of the bill, inasmuch as the liquidation of the bank was being carried on by the State Banking Commissioner under the supervision of the New Hampshire Courts. It was admitted that the federal court had jurisdiction. It was stated, how-

ever, that since the original proceeding against the bank in the state court was a proceeding in rem, and involved the exercise of possession or control over the fund in the custody and possession of the Commissioner, the Federal Court should decline to exercise jurisdiction over the controversy. The opinion points out that the effect of the prior proceeding in the state court is to draw to that court (p. 383)—

> "the possession or control, actual or potential, of the res and the exercise by another court of jurisdiction over the same res necessarily impairs, and may defeat, the jurisdiction (that has already attached) of the court in which the prior action was brought."

It is, therefore, no answer to appellee's contention to assert that the Secretary of Banking is not a receiver, and that the doctrine of comity between courts does not apply. This argument, carried to its logical conclusion, conflicts with the decision in *Pennsylvania v. Williams, supra.* If the Secretary, because he may not be technically a receiver, is not entitled to have determined in the state courts all questions incident to the preservation, collection and distribution of the assets, there is no reason why a federal court, in addition to determining those questions, should not appoint receivers to take charge of the entire liquidation.

Nor can it be contended that the present action can be converted into one in personam and not in rem by molding the decree of the Court so as to adjudicate only the right to the fund, omitting any direction to the Secretary to pay it over to the complainant. In this way, it is claimed, the state court can still adjudicate final disposition of the fund, in accordance with the federal court's order. The

vice in this proposition lies in the requirement that the Secretary must defend extensive litigation in the federal courts and convert himself from a stakeholder into a litigant. As heretofore pointed out, this result does violence to the scheme of the State statute as interpreted by the state court Compare *Franklin Trust Company's Case, supra.* Moreover, the time for filing preferred claims in the state court has long since expired. A decree of this Court directing the Secretary of Banking to accord to appellant a preference in whatever assets of the Franklin Trust Company may now remain in his hands is, consequently, requiring him to violate the State statute by paying a preferred claim barred by that statute.*

If the Secretary of Banking be held to have the status of a receiver of the state court, the difficulties noted above could be avoided through the refusal of a federal court to entertain jurisdiction of a suit against the Secretary as receiver unless permission of the state court was first obtained. This is the rule in receivership cases. *Porter v. Sabin,* 149 U. S. 473; *Barton v. Barbour,* 104 U. S. 126; *Merrywcather, et al. v. United States,* 12 F. (2d) 407 (C. C. A. 9th) 1926; *Mullendore v. American Surety Co. of New York,* 27 F. (2d) 572 (C. C. A. 9th) 1928. No attempt was made by appellant in the present proceedings to secure the consent of either the Secretary of Banking or the state court to the institution of the present proceedings in the United States District Court.

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*This does not mean that appellant would not receive depositor's status in the state court. Section 42 of the Act (Appendix, p. 92) requires that all claims other than those of depositors shall be filed within four months of the date of notice of taking possession by the Secretary. Depositors, however, are not required to file claims if they appear as such on the books of the institution, which, of course, appellant does.

Appellant relies on the line of cases represented by *Byers v. McAuley*, 149 U. S. 608; *Waterman v. Canal-Louisiana Bank & Trust Co.*, 215 U. S. 33; and *Commonwealth Trust Co. v. Bradford*, 297 U. S. 613 (1936) to sustain its contention that the District Court was required to entertain jurisdiction of the litigation. Those cases hold that suits may be instituted in the federal courts against executors and trustees who are subject to the supervision of state probate courts to establish claims against decedents' estates and other property held in trust. The distinction between these cases and the liquidation of an insolvent banking institution by an officer of the State was summarized in the last cited case as follows (p. 619):

> "The doctrine approved in Pennsylvania v. Williams, 294 U. S. 176, 79 L. Ed. 841, 55 S. Ct. 380, 96 A. L. R. 1166, and Penn General Casualty Co. v. Pennsylvania, 294 U. S. 189, 79 L. Ed. 850, 55 S. Ct. 386, supra, is not applicable. In each of those cases we found conflict between the Federal Court and authorities of the State concerning liquidation of the business and assets of an insolvent local corporation. The question was whether, under the peculiar circumstances disclosed, the Federal Court should retain jurisdiction; its power generally to render judgment in personam against fiduciaries appointed by State Courts was expressly recognized. Here there are no extraordinary circumstances."

This Court, in the *Bradford* case, differentiated receivership cases from those involving the administration of decedents' estates on the ground that, in the latter class of cases, the property is not in custodia legis. If, as pointed out above, the Secretary of Banking is entitled to the status of a receiver, it would seem to follow that the property in his possession, which is subject to the control of the State

Court, is sufficiently in custodia legis to sustain the distinction.

Nor does *Riehle v. Margolies, supra,* aid the appellant. In that case, this Court held that a suit instituted against a corporation in a state court, prior to the appointment of receivers for the corporation in the federal court, could be prosecuted to judgment and would be res judicata as to the validity of the claim when the judgment was presented in the court of the receivership. No question of the equitable discretion of a federal court to determine for itself whether or not to entertain jurisdiction was involved. The claim sued on in the state court was a contract liability, which was clearly in personam. No attempt was made to interfere in any way with the possession and control of the res constituting the assets of the corporation by the federal court. It could be admitted that if, in the present proceedings, this Court should determine that the District Court was correct in entertaining jurisdiction of appellant's Bill in Equity and should reverse the Circuit Court of Appeals on the merits, the final decree would be res judicata when presented in the liquidation proceedings in the State Court. That is all that is suggested by *Riehle v. Margolies,* although even this result would not necessarily follow in the present case because here the jurisdiction of the state court was invoked before the federal litigation began. The vital question, however, remains whether the Federal Court should entertain jurisdiction of appellant's bill. For the reasons above set forth, it is submitted that the answer should be in the negative.

(d) *Summary of argument on jurisdiction.*

Appellee contends that the Circuit Court of Appeals for the Third Circuit correctly decided that jurisdiction of

appellant's Bill in Equity should not be entertained. In *Pennsylvania v. Williams*, supra, this Court decided that the federal courts should not interfere with the method of distribution of the assets of semi-public corporations of a State, being liquidated by a State officer under a comprehensive State statute, by appointing federal receivers to liquidate such assets. In *United States v. Bank of New York & Trust Co., supra,* this principle was extended so as to preclude determination by the federal courts of suits brought for an accounting and turning over of the assets in the hands of the statutory liquidator of the state court. It is urged that the same principles should restrain the federal courts from passing on a controversy involving an attempt to establish a trust in and compel the payment to appellant of, part of the assets held by a State statutory liquidator, acting under the supervision and control of a state court. Otherwise, it is submitted, the principles of the above cases will lose all significance and the State system of liquidation be impeded and delayed.

It is further urged that jurisdiction should be refused because indispensable parties, i. e., the depositors and other creditors of the insolvent Franklin Trust Company, are not before the Court. If jurisdiction of appellant's Bill is entertained under such circumstances, the statutory liquidator would be converted from a stakeholder, which is his status under the State law, into an active party litigant. Such a result does violence to the State scheme of liquidation and distribution.

Finally, it is suggested that the present proceeding is analogous to an action quasi in rem brought in one court against the receiver of another court, which has already assumed jurisdiction of the res. On familiar principles of

receivership law, it is submitted that the second court will refrain from entertaining jurisdiction over such a bill.

Therefore it is respectfully submitted that the decree of the Circuit Court of Appeals for the Third Circuit entered on September 11, 1936, as corrected by the decree entered on October 16, 1936, directing the District Court for the Eastern District of Pennsylvania to dismiss the bill on jurisdictional grounds should be affirmed.

II. The Circuit Court of Appeals for the Third Circuit and the District Court for the Eastern District of Pennsylvania properly dismissed appellant's bill upon the merits.

Appellant seeks to assert a preference of $40,842.51 composed of cash deposited in Franklin Trust Company prior to its closing; $8,747.66, the proceeds of checks and drafts deposited in Franklin Trust Company; and $32,403.26, a total of cash, drafts and checks deposited in the correspondent banks of Franklin Trust Company. Appellant asserts a preference in the $40,842.51 cash on the ground that a trust relationship as to it existed between Franklin and appellant. Its assertion of a preference as to the checks in Franklin Trust Company and the checks, drafts and cash in the correspondent banks, is predicated on other grounds. All of these deposits, however, both checks and cash, and in both Franklin Trust Company and its correspondent banks, were made pursuant to the oral agreement of August 25, 1925, as modified in 1930. The checks and cash deposited in Franklin itself were deposited pursuant to clause (c) of the agreement, and the checks and cash in the correspondent banks were deposited pursuant to clause (d) of the agreement. Appellant and appellee differ as to the terms of these clauses, but whether appellant's

or appellee's version of the agreement be accepted, it is evident that the checks deposited in Franklin Trust Company and the checks, drafts and cash deposited in the correspondent banks selected by Franklin Trust Company became as much a part of the deposit account in Franklin as the cash deposited in Franklin itself. This is shown by the fact that the deposits made by appellant in the correspondent banks pursuant to (d) were deposited to the credit of and subject to the check of Franklin Trust Company only; by the fact that such deposits were credited by Franklin Trust Company in the same "deposit account" made up of deposits in the Franklin Trust Company itself by appellant pursuant to (c) of the agreement; and by the fact that the cash funds were to be made available to appellant in the amount credited to appellant in the one "deposit account" including such credit. [R. pp. 31-32, 48.] It follows, therefore, that any trust relationship to be predicated on the deposit of cash in Franklin must apply equally to all the cash, checks and drafts deposited in both Franklin and the correspondent banks, and appellee's argument will be based on that premise. Appellant's other grounds for preference, as to checks deposited in Franklin and the checks, drafts and cash deposited in the correspondent banks, will be considered later.

(a) *The Deposits of Checks, Drafts and Cash by Appellant in the Franklin Trust Company and the Correspondent Banks Gave Rise to a Debtor-Creditor Relationship and Appellant Has Therefore Only a Depositor's Status.*

The funds in which appellant claims a preference were actual deposits; the agreement specifically stated that they were to go into a "Deposit Account". It is fundamental

that deposits made in ordinary course of business create the relation of debtor and creditor between bank and depositor so that upon insolvency of the bank the depositor is entitled only to a pro rata share in its assets along with other claimants of the same class. If this debtor-creditor relationship is not to arise, the depositor must establish that by the terms of the agreement of deposit the bank was not to have the use of the funds but was to hold them in trust for the benefit of the depositor and segregated from its general funds.

> "It is no longer an open question in this court, since the decision in the cases of *Marine Bk. v. Fulton Bk.*, 2 Wall., 252 (69 U. S., XVII., 785), and of *Thompson v. Riggs*, 5 Wall., 663 (72 U. S., XVIII., 704), that the relation of banker and customer, in their pecuniary dealings, is that of debtor and creditor. It is an important part of the business of banking to receive deposits, but when they are received, unless there are stipulations to the contrary, they belong to the Bank, become part of its general funds, and can be loaned by it as other moneys. The banker is accountable for the deposits he receives as a debtor, and he agrees to discharge these debts by honoring the checks which the depositors shall from time to time draw on him. The contract between the parties is purely a legal one and has nothing of the nature of a trust in it."
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> *The National Bank of the Republic v. Millard*, 177 U. S. 152, 19 L. Ed. 897.

> "We think, ... that it is the necessary effect of the Supreme Court cases cited that the presumption that arises from the very nature of the banking business of a right to use deposited funds in the general business of the bank where there is absent any expressed or clearly implied intention otherwise precludes us from sustaining the conclusion of the court

below that the fund here in question was a special deposit, or became impressed with a trust."

Keyes v. Paducah & I. R. Co., 61 F. (2d) 611.

"Whether a deposit in a bank is general or special depends upon the contract resulting from the mutual understanding and intention of the parties at the time such deposit is made. Fogg v. Tyler, 109 Me. 109, 82 A. 1008, 39 L. R. A. (N. S.) 847, Ann. Cas. 1913E, 41; 3 R. C. L. § 146, p. 517. But a deposit made in the ordinary course of business is presumed to be general, and the burden of proof is upon the depositor to overcome such presumption by proving that the deposit was made upon such terms and conditions as to constitute it a special deposit or a deposit for a specific purpose, as distinguished from a general deposit." (Citing cases.)

Northern Sugar Corp. v. Thompson, 13 F. (2d) 829.

"If money is deposited in a bank for a special purpose, the bank is a trustee or bailee of the money if, but only if, it is the understanding of the parties that the money deposited is not to be used by the bank for its own purposes."

Restatement of the Law of Trusts, § 12, Comment h, p. 46.

See also *Commercial National Bank v. Armstrong*, 148 U. S. 50, 37 L. Ed. 363; *Marine Bank of Chicago v. Fulton County Bank*, 69 U. S. 2, 17 L. Ed. 785; *Thompson v. Riggs*, 72 U. S. 663, 18 L. Ed. 704; 7 C. J. 630; 3 R. C. L. 517; *Morse, Banks and Banking*—Vol. 1, § 186.

Appellant has not established that its agreement with Franklin Trust Company constituted its deposits special rather than general. There is absolutely no language in the agreement providing that the funds deposited were to be held in trust or that they were to be segregated and not

mingled with Franklin's general funds and used by it in its banking business.

Having no express agreement to that effect, appellant seeks to alter the general rule by setting up a number of inferences that Franklin was not to have the use of the funds deposited in the account. Not only are these inferences insufficient in themselves to vary the usual rule that the bank is to have the use of deposits made with it, but they are in point of fact rebutted by the agreement itself.

First, appellant argues that clause (e) of the agreement expressly established under what terms and conditions Franklin Trust Company would be allowed to use the cash entrusted to it. Clause (e) provided that appellant might enter into oral agreements with Franklin Trust Company whereby Franklin Trust Company would be permitted to use the funds deposited pursuant to clauses (c) and (d) of the agreement for certain periods of time, these sums to be called by petitioner's check only, instead of being forwarded by Franklin Trust Company. This clause further provided that under such agreements and no other would said fund ever become subject to check. Appellant argues that since this was a special agreement for Franklin to have the use of the funds at certain times, it could not have had the use of the funds in the absence of such agreement. This is a very weak inference. As a matter of fact such an agreement is perfectly consistent with what was the fact, that Franklin was to have the use of the funds in any event but the operation of clause (e) gave it the use of the funds for a longer period of time. Clause (e) is a straw showing which way the wind blows. That a voluntary agreement might be made permitting the funds to be used for a longer period of time than theretofore permitted is not nearly so

surprising as a voluntary agreement to permit the use of funds which without such agreement must be absolutely segregated. A change of time in the use of a deposit is far different from a change in the character of a deposit. Judge Kirkpatrick in the District Court took the view that clause (e) merely meant that the funds were to be used for a longer period of time. In his opinion (R. 24, 25) he said:

> "The fact that the parties contemplated and actually made subsequent arrangements by which large amounts of money in the deposit account were allowed to remain with the Trust Company for considerable periods without anything being said or done as to change the character of the deposit or the relationship created thereby is more than merely suggestive. What could be the purpose of these special arrangements unless it was understood all along that the money on deposit was being used by the Trust Company in its general banking business and it was desired to give them the use of more money for a longer time?"

It follows therefore that any inference from the agreements made under clause (e) that the deposit account was special must fall.

Next, appellant argues that since 2% interest was to be allowed by Franklin on the disbursement account and no interest was to be allowed on the deposit account, it is to be inferred that Franklin was not to have the use of the funds placed in the deposit account. The receipt of interest, however, is not the only method by which a depositor may be compensated for permitting a bank to use his funds. Here, appellant was compensated for permitting the use of these funds by itself obtaining the use of Franklin's banking facilities, by which it was enabled to have made

available to it at its New York office all the collections made by its distributors, not only in Philadelphia but in a number of other cities in Pennsylvania, New Jersey and Delaware. Appellant states on page 36 of its brief that—

> "It is inconceivable that business men of the acumen to require 2 per cent. interest on a checking account would forego interest or money on deposit in another account with the same bank, if they intended the bank to have the same right to use the funds therein."

Appellant fails to consider that banking officials are also supposed to have acumen and that the furnishing of banking facilities in return for the use of funds is the only way that a bank can make money. If it makes too much, the law of supply and demand will necessitate a rebate of part of it by the payment of interest. The fact was that Franklin thought—and agreed—that for what it furnished appellant it was entitled not only to a steady disbursement account upon which it was willing to pay 2% interest until the modified agreement of August, 1930, because it was steady but that, in addition, it should have the use of the funds placed in the deposit account because of the work it was doing. And, since appellant received this consideration —the use of Franklin's facilities—no inference can be drawn from the failure of Franklin to pay interest on this deposit account that it was not to have the use of the funds, especially in view of the fact that the use of them was for very short periods of time. As a matter of fact, every inference is the other way. The attention of the Court is called to Exhibits A and C of plaintiff's bill. (R. pp. 39-42.) These exhibits are two letters written by Franklin to appellant dated June 12, 1925, and August 22,

1925, prior to the time the oral agreement was entered into. In each of these letters Franklin outlined the program: its proposal to collect the deposits in and about Philadelphia for appellant, to deliver weekly payrolls to the appellant's branches, to arrange for deposits to be made by appellant's distributors in correspondent banks selected by Franklin in neighboring towns. In the letter of June 12, after outlining what it proposed to do, Franklin stated (R. p. 40):

> "*In consideration of the above* it is our understanding that you will maintain with us a general account, wherein all moneys collected will be deposited, the entire balance of which we will remit to you weekly; also an active checking account, the funds to be deposited from your main office, the balance to be maintained on an average of not less than $25,000.00, which will receive interest at the rate of 2% per annum." [Italics supplied.]

In its letter of August 22nd Franklin likewise stated (R. p. 41):

> "*In consideration of the above* it is our understanding that you will maintain with us two (2) accounts, one to be known as the Deposit Account, and the other to be known as the Disbursement Account. The Deposit Account is for the purpose of handling daily collections. All monies received from your Philadelphia plants and out of town distributors are to be put into this account, and on Monday morning of each week we will transfer the previous week's total of collections, either through our Federal Reserve correspondent, or through our direct New York correspondent bank, whichever we conclude to be the most effective for your purpose, so that cash funds to the amount of such weekly collections will be to your credit by every Monday at 3 o'clock in the afternoon." [Italics supplied.]

From these two letters it is clear that Franklin considered that it was to have the use of both accounts as consideration for its placing its facilities at appellant's disposal. So far as the Record shows, appellant never made any effort to disabuse Franklin of this thought.

It should be noted that the words "collected" and "collections" as used in those letters refer to the picking up of cash, checks, etc., by representatives of Franklin from the various plants of appellant and not to the "collection" of the checks and drafts from the drawee banks through ordinary banking channels.

Next, appellant argues that no provision of the agreement between the parties suggests that Franklin Trust Company had the right to use these funds except when the parties expressly so agreed. But here the shoe is on the other foot. Appellant was dealing with a bank and it was bound to know that, if it did not wish the bank to make use of the funds in accordance with the universal practice of the banking business, it should have expressly so stipulated. This is hornbook law, as is indicated by reference to the authorities heretofore cited in this brief at pages 36-37. Therefore, since the agreement is silent on the point as to whether Franklin was to have the use of the funds deposited, the only inference that can be drawn is that Franklin was to have such use.

Next, appellant argues that when it did let Franklin use sums for a longer time than usual under clause (e) of the agreement, said sums were to be called by check instead of being forwarded by Franklin to appellant in New York City, whereas, otherwise the account was never subject to check but was to be forwarded to petitioner in New York. From this appellant desires the inference drawn

that cash was to be forwarded and no checking to be allowed, and that therefore the actual cash deposited was to be set aside as trust property and not subject to the usual incidents of a general deposit. This argument can be readily answered. In the first place appellant's inference is itself based upon another untenable inference that cash was actually to be shipped from Philadelphia to New York. See pages 45 ff. *infra*. Moreover, to have provided for checking out these funds would have defeated the purpose of the agreement, which was to use Franklin's facilities so that funds collected in Philadelphia and other towns would be made available to appellant in New York City on a certain day. The question is whose funds were to be made available—Franklin's or appellant's? Every inference and every applicable rule of law show that Franklin was merely giving its general obligation to have funds made available in New York. But in any event, as stated above, the failure to provide for checking privileges has no bearing on the intention of the parties as to the use of the funds. As a matter of fact, any inference from this circumstance would favor the bank because by the agreement it was assured that these funds need not be made available until the following Monday and that it, therefore, had the absolute and safe right to use the funds meanwhile without fear of its account being suddenly checked against by appellant.

Next, appellant argues that since it was not required to maintain an average balance in the so-called "deposit account", while an average balance had to be maintained in the "disbursement account", an inference is to be drawn that Franklin had not contemplated the use of the funds in the deposit account. No such inference can be drawn. Franklin had contemplated the use of the funds in the de-

posit account (see pp. 39-42 *supra*) but it may be presumed that since it would have the use of these funds for such short periods of time and since the amount of the funds in the deposit account was not certain, it was not being adequately compensated for its services unless it was assured that a general average balance would be maintained with it. See "Exhibits A" and "C" [R. pp. 39-41]. It did not matter to Franklin Trust Company whether this average balance existed in the "disbursement account" or in the "deposit account". The main thing was that Franklin be assured a general average balance. The giving of different names to different accounts was done for appellant's convenience and to facilitate its bookkeeping.

Finally, appellant argues that it is not to be inferred that Franklin was to have the use of these funds in the deposit account because it (Franklin) received ample consideration for its services, both in the maintenance of the $25,000 balance in the disbursement account and in the agreement of appellant unde clause (e) to leave large sums on deposit with Franklin in such amount and for such period of time as appellant might feel disposed. From the standpoint of actual consideration, the event proved that there was little that Franklin could count on in the way of acquiring the use of funds for additional periods of time, as provided by clause (e) of the agreement. As a matter of fact, in only five months out of the six years in which the agreement was in effect did appellant leave large sums on deposit with Franklin pursuant to this agreement. [R. p. 34.] All that Franklin could be assured of was the $25,000 general balance in the disbursement account and such sums as might come into the deposit account for very short periods of time. Moreover, it is not for the Court to say on the pleadings just what consideration was sufficient for

Franklin to repay it for its services. Franklin was entitled to the consideration that it bargained for, regardless of amount, and the bargain in this case was made after considerable dickering on both sides, as the exhibits show.

In the last analysis, appellant contends that because it agreed to deposit cash in the Franklin Trust Company and Franklin agreed to provide cash for it in New York, a trust relationship as to that cash is to be implied. To this argument there are two answers:

1. Franklin Trust Company's obligation to furnish funds to appellant in New York City was based on and measured by the amount of the "deposit account" established by clause (c) of the agreement. The amount of this "deposit account" was made up by Franklin's crediting to it (1) the amount of the cash and checks deposited by appellant in Franklin Trust Company itself and (2) the amount of the cash and checks deposited by appellant in the correspondent banks pursuant to clause (d) of the agreement. That the "deposit account" referred to was composed of deposits made in correspondent banks as well as in Franklin is clear even if appellant's version of the facts be taken. On page 4 of its Brief appellant says with respect to the agreement:

> "(c) Franklin Trust Company would accept from petitioner's distributors in Philadelphia, cash, also drafts and checks for collection, for the purpose of forwarding the cash, together with the proceeds of the drafts and checks, on Monday of each week to petitioner, or its depository, in New York City; said account to be known as a 'Deposit Account'.
>
> "(d) Franklin Trust Company would select, subject to the approval of petitioner, certain correspondent banks in neighboring towns and cities in New Jersey,

> Delaware and Eastern Pennsylvania, to accept, from distributors of petitioner, cash, drafts and checks to be credited to, and subject to the check of Franklin Trust Company only, but earmarked as the funds of petitioner; a written acknowledgment of receipt of said cash, drafts and checks by each of said correspondent banks to be mailed immediately upon receipt of same to petitioner in New York City, and . . . *all cash, drafts and checks accepted by said correspondent banks were to be credited to the said deposit account referred to in Clause (c) above,* for the purpose of Franklin Trust Company forwarding the cash and the proceeds of the drafts and checks, together with the amount referred to in Clause (c) above, on Monday of each week, to petitioner, or its depository, in New York City." (Italics supplied.)

Part of the "deposit account", then, was based on deposits in the correspondent banks, which deposits were credited by those banks to Franklin. There is nothing in the Record, however, to show that Franklin was to receive cash from the correspondent banks and it is to be presumed that the major portion of the deposits in these banks was never paid over to Franklin. Most of them would, in the normal course, be taken care of by the usual method of cancelling mutual credits and debits, only occasional balances between the banks being settled in cash. For the credit it obtained in the correspondent banks, Franklin substituted its own obligation to appellant by crediting the "deposit account". To that extent, the funds furnished by Franklin to appellant in New York were necessarily Franklin's funds and not the funds of appellant. Thus, the picture that appellant would like to present of a simple arrangement of receiving cash in one hand, transferring that cash to another hand and dropping the cash from that

extended hand into a depository in New York is actually non-existent. As far as the deposits in the correspondent banks are concerned, Franklin was obliged to dig into its own pocket to make cash available to appellant in New York in return for the credits which Franklin had received in those banks.

2. Even as to the cash deposited by appellant in Franklin Trust Company itself, the parties never agreed and in fact never contemplated that it would be actually set aside by Franklin and shipped intact to New York. All that was expected—and all that was bargained for—was that Franklin would by the use of the banking facilities of its correspondents in New York make the necessary funds available to appellant in that city. The correspondence between the parties ("Exhibits D" and "E"), written after the agreement was made, clearly shows that appellant knew and acquiesced in Franklin's method of handling the account. These exhibits consist of a letter dated September 9, 1925 written by appellant to Franklin and a reply to that letter dated September 11, 1925 by Franklin to appellant. This letter of appellant to Franklin was in the nature of a complaint because it had not actually received cash in New York on Monday afternoon but had received instead a cashier's check of the First National Bank of New York. [R. p. 43.]

Franklin's letter, Exhibit E, contained an apology for this and informed appellant that it was the fault of the First National Bank of New York, Franklin's New York correspondent in the matter, and that the First National Bank of New York had departed from instructions in not furnishing cash funds. [R. p. 44.]

It is obvious from this correspondence that appellant knew that it was not getting in New York the actual cash deposited in Philadelphia but cash made available to it by Franklin through its New York correspondent and that it was satisfied with the method that Franklin used to perform its obligation provided that cash funds either from Franklin's New York correspondent or from some other source were made available to it in New York at the specified times. This action of Franklin was consistent with the understanding of the parties during the negotiations leading up to the oral agreement. In the letter of August 20, 1925 (R. p. 40B) appellant, after informing Franklin of the accounts to be set up, stated:

> "On Monday of each week it is understood we will receive from you in cash funds the balance of the three deposit accounts as of the close of business the previous Saturday night. As to the method of transfer, we would be very glad to follow your suggestions and in the event that you may wish to make the transfer direct to our New York depositary the American Exchange-Pacific National Bank, 128 Broadway, New York City, we ask that a memoranda of the transactions for the week covering the transfer be mailed direct to this office for purposes of reconciliation with our records."

In its letter of August 22, 1925, Exhibit C (R. p. 41) Franklin stated:

> ". . . All monies received from your Philadelphia plants and out of town distributors are to be put into this account, and on Monday morning of each week we will transfer the previous week's total of collections, *either through our Federal Reserve correspondent, or through our direct New York correspondent bank,* whichever we conclude to be the most effective for your

purpose, so that cash funds to the amount of such weekly collections will be to your credit by every Monday at 3 o'clock, in the afternoon." (Italics supplied.)

These letters show that in these negotiations appellant contemplated that Franklin would use the ordinary banking methods of making funds available to it and, in view of the fact that appellant did not object to these methods, it is evident that it was satisfied with them. The letters written after the agreement was entered into—Exhibits D and E to the Bill—show that appellant did not object to Franklin's using these banking facilities provided, as has been said, Franklin saw to it that cash was made available to it in New York—not the cash formerly owned by appellant but cash whose source was the general funds of the Franklin Trust Company.

Since the Franklin Trust Company and appellant expressly agreed that Franklin was to perform its obligation to appellant by using its own funds, it follows—and, as has been shown, the parties so agreed—that Franklin was not to keep segregated the funds deposited by appellant but was, in accordance with the universal practice of banks, to mingle them with its own funds and use them in its business. It follows further that the relationship between the parties was a contractual and not a fiduciary one. If a depositor wishes to establish a fiduciary relationship between a bank and himself rather than the customary debtor-creditor relationship, he must bargain for the fiduciary relationship by stipulating with the bank that his funds are to be set aside and not to be used by the bank. As Mr. Justice Stone said in his article *Some Legal Problems Involved in the Transmission of Funds,* 21 Columbia Law Review 507, written when he was Dean of Columbia Law School (at pages 513-514):

"When the transaction involves the banker's undertaking to procure the payment at a distant point the customer is often spoken of by bankers and in judicial opinion as having 'purchased' exchange, but it is obvious that the term 'purchase' when applied to such a transaction where the banker does not deliver a bill or draft to the customer is a mere figure of speech and all that the customer has actually purchased is the banker's undertaking or obligation to effect the payment at a distant point. . . . Thus the merchant or traveller who wishes to establish a credit in a foreign country and secures it by payment of money in dollars to his banker, speaks of having purchased pounds sterling, francs, or lire, as the case may be, although all that in fact or in law he has actually secured is some kind of an obligation by the banker to secure credit at the distant point payable in pounds, francs, or lire, as the case may be. Even when the obligation is performed and the credit is established, he is still only the owner of an obligation or *chose in action,* and not of *any actual foreign* money.

"Nor would the customer be justified in supposing that moneys deposited with the bank in order to ensure payment at a distant point would be dealt with by the banker in any different manner than in the case of other moneys deposited with the banker by his general customers. Moneys thus deposited are commingled with the general funds of the banker and dealt with by him as his own funds to be paid out in the course of his banking business which is publicly known and understood to be a business conducted for profit, and in general the customers in dealing with the banker and in the absence of express stipulation deal with him in reliance on his personal credit and not on the presence in the banker's hands of any specific fund to which he may assert a claim. Moreover the difficulties of transacting exchange business by maintaining a segre-

gated fund for each customer until the transaction is completed would be practically insuperable.

"Assuming that the transaction is not the exceptional one of bailment, does the banker who undertakes the transmission of funds in the ordinary course of the banking business become a fiduciary or is he a mere debtor or contractor who undertakes to discharge his debt by payment to a third person? If one bears in mind the elementary principles of banking hereinbefore referred to, which are of universal application, and the established custom of bankers in dealing with funds received in the ordinary course of business, the inference would seem to be irresistible that the undertaking of the banker was not fiduciary but is in the nature of a contractual obligation. The banker being engaged in a business whose very existence depends on the customary and rightful use of funds entrusted to him, as the banker's own, and the universal custom in practice being the use of such funds as the banker's own and their transmission by a system of credits only, the ordinary presumption that funds received for account of another are held in fiduciary capacity should not apply."

It may be conceded that appellant had a particular purpost in mind in making these deposits and that Franklin knew of that purpose. That is not enough. To make Franklin a fiduciary for that purpose, appellant was bound to stipulate, expressly or impliedly, that Franklin act as a fiduciary by segregating the funds to accomplish the purpose; and having failed to so stipulate, it merely acquired Franklin's general obligation to perform, and, consequently, became Franklin's creditor only. The fatal effect of a depositor's failing to stipulate for segregation of his funds and his consequent failure to acquire a cestui que

trust's status even where he made his deposit in the bank for a particular purpose is shown by the recent decision of the United States Supreme Court in *Blakey v. Brinson,* 286 U. S. 254, 76 L. Ed. 1089 (1932).

In that case Brinson had a deposit of $1961.31 in his savings account in the First National Bank of New Bern, North Carolina. On October 10, 1929, an officer of the bank told Brinson that the bank would purchase $4000 worth of United States Bonds for him and asked him to bring to the bank on October 14th such amount in addition to his credit balance as would be required to pay for the bonds. On October 14th Brinson deposited a check for $2100, bringing his deposit balance to more than $4000. Brinson was informed that his bonds had been purchased and his deposit account debited, and that the bonds were held in a bond account. When the bank closely shortly afterward, it was discovered that no bonds had ever been purchased, ordered or received for Brinson. Brinson brought suit against the Receiver of the bank and the district court held that the $4000 necessary to purchase the bonds was held in trust for the purpose of purchasing the bonds and that Brinson should therefore receive a preference over other creditors of the bank. This decision was affirmed by the Circuit Court of Appeals but was reversed by the United States Supreme Court. The Court held that only a debtor-creditor relationship existed between the bank and the depositor and that therefore depositor was entitled to no preference over other claimants upon insolvency. The mere fact that depositor had turned over his funds for a particular purpose, namely, the purchase of bonds, did not give rise to a trust relationship where he did not establish that the bank had undertaken to segregate and use his own funds rather than

to give its general obligation to purchase the bonds with its funds. Said the Court (p. 260):

> "It would have been equally competent for respondent to have provided for the purchase of the bonds either by the creation of a trust of funds in the hands of the bank, to be used for that purpose, or by establishing with it a credit to be debited with the cost of the bonds when purchased. But only if the former was the method adopted could respondent, upon the bank's insolvency and failure to purchase the bonds, recover the fund or its proceeds, if traceable, in preference to general creditors, see Minard v. Watts (C. C.) 186 Fed. 245; Fallgatter v. Citizens' Nat. Bank (D. C.) 11 F. (2d) 383; Northern Sugar Corp. v. Thompson (C. C. A. 8th) 13 F. (2d) 829."

Blakey v. Brinson is remarkably like the instant case not only in principle but also on its facts. In that case the Court saw no justification for turning the chose in action of $1961.31—i. e., the pre-existing deposit—into a specific res by imposing the duty of segregating that amount upon the bank when it received the additional deposit of $2100. from Brinson, which latter deposit was made only for the purpose of purchasing the bonds. The court held that since the $2100. was placed with the bank in the form of a deposit, the inference was that it was in fact a deposit to be added and become part of the former deposit, to make one large chose in action of $4,061.31. As to his earlier deposit, if Brinson wanted a segregation at this late date he should clearly have so specified. Without such segregation, a segregation of the later $2100 would not have advanced his purpose. Therefore, an agreement to segregate, even the $2100 deposited, was not to be inferred merely from the statement of his purpose in making the deposit. As the Court said (p. 261):

> ". . . Respondent obviously did not alter the debit and credit relationship with respect to the $1,961.31 balance by asking the bank to purchase bonds, or by handing to the bank the deposited check of $2,100. All that happened on that date was inconsistent with any purpose to create a trust of the check or its proceeds, and showed unmistakably that the amount of the check, as in the case of any other deposit in the savings account, was to be added to the existing balance and treated like it."

In this respect *Blakey v. Brinson* is remarkably analogous to the present case. It is true that cash was deposited in the Franklin Trust Company with the understanding that cash would be supplied to appellant in New York City but the amount that appellant was to receive in New York on Mondays was, as has been shown, the *total* of the so-called deposit account and this account was made up not only of the cash deposited in the Franklin Trust Company but also of funds deposited in correspondent banks, credit advices of which were sent to Franklin Trust Company. There is absolutely nothing in the Record to show that cash was forwarded to Franklin Trust Company by these correspondent banks. The inference is rather that Franklin Trust Company merely received credits and that balances were adjusted between Franklin Trust Company and these banks only occasionally. Therefore, to the extent that the "deposit account" in Franklin was based on deposits made in the correspondent bank by appellant, it—the "deposit account"—*could not* have been more than a general obligation of Franklin to appellant. For, to create a trust in the account as to such deposits in the correspondent banks Franklin would have had to take its own cash, not deposited by the claimant, and seg-

regate it as a trust res. Nowhere in the agreement is there any suggestion that a segregation of Franklin's own funds to cover such credits in correspondent banks should take place and an obligation to segregate such funds should not be inferred. On the contrary, the inference in the present case, just as it was in *Blakey v. Brinson,* is that the funds actually deposited in Franklin Trust Company were to become its property in exchange for the general obligation of the Franklin Trust Company because the funds actually deposited became, without differentiation, a part of a greater deposit account, part of which—a mere chose in action—could not, for the reasons stated, be anything more than a general obligation of the Franklin Trust Company.

Cases like *Blakey v. Brinson* and the present case arise either because a depositor is ignorant of the functions of the bank or because, if the depositor is aware of its functions, he thinks his particular facts take on a color that sets his deposit apart from the rest of the depositors. It may be that Brinson thought he was creating a trust because he had a particular purpose in mind but since he did not stipulate for a trust and since he turned his funds over to the bank by making use of the usual deposit account, he is bound by the legal effect to be given to such an agreement, namely, that the bank becomes his debtor and he becomes the bank's creditor. Exactly the same thing is true in the present case. The appellant made its deposits with Franklin for six years and never asserted any formal requirement that funds were to be segregated. In fact, there is no evidence that it ever wanted anything except what it got as the result of the agreement made with Franklin, that is, the general obligation of Franklin to make funds available to appellant at the required time. As Justice Holmes said in *Equitable*

Trust Co. v. First National Bank, 275 U. S. 359, 368, 72 L. Ed. 313, 316 (1928):

> "People dealing with large banks do not ordinarily seek the ambiguous security of an identified fund, they are satisfied if the bank gives them credit."

It is only when the bank fails, as in this case, that the depositor fastens on small phrases in the agreement in order to set himself apart from the rest of the depositors when, as a matter of fact, his agreement was actually such that his deposits became the funds of the bank as did the deposits of everyone else except those who could and did stipulate with the bank that it was to hold in trust the moneys placed by them in the bank's custody.

The *Equitable Trust* case, *supra,* like *Blakey v. Brinson,* holds that the failure of a depositor to stipulate that a fund is to be segregated is fatal. That case differs from *Blakey v. Brinson* only in that the purpose of the deposit in the *Equitable Trust* case was for "transmission" of funds, whereas in *Blakey v. Brinson* the purpose of the deposit was to purchase property for the depositor. The facts in the *Equitable Trust* case were as follows:

The subsequently bankrupt firm of Knauth, Nachod & Kuhne had credit with many foreign banks and for a consideration furnished this credit to smaller banks in the United States, as a result of which these small banks could draw directly upon the foreign banks. The terms offered to such banks by the bankrupts were (p. 365):

> "Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance,

or otherwise, provided the draft is drawn on a bank named in our latest list of correspondents."

The First National Bank drew a draft on one of the foreign banks, notified the bankrupts that they had sold it, asked them to protect the same on presentation and remitted a check to the bankrupts. The bankrupts on the same day sent to the foreign bank a list of the drafts issued with the request that such drafts be honored by the foreign bank and charged to the bankrupts' account. The foreign bank on receiving this notice debited the account of the bankrupts with it. The understanding between the foreign bank and the bankrupts was that such advices could be canceled at any time and the bankrupts' general account recredited. When the drafts sold were presented to the foreign bank, they were dishonored because Knauth, Nachod & Kuhne had become insolvent. The First National Bank, having been forced to take up the drafts it issued, filed a claim for preference against the assets of the bankrupts upon two theories. It contended first that the sum paid to the bankrupts was paid upon trust for the purpose of being applied to honor the draft. This is in substance the same theory that the appellants have raised here under their third proposition. This contention was dismissed summarily by Mr. Justice Holmes in the following words (p. 366):

"The first of these need not detain us. Beecher v. Cosmopolitan Trust Co., 239 Mass. 48, 131 N. E. 338; Legniti v. Mechanics & Metals Nat. Bank, 230 N. Y. 415, 16 A. L. R. 185, 130 N. E. 597. The identity of the fund was not maintained and no one expected it to be. See National City Bank v. Hotchkiss, 231 U. S. 50, 56, 57, 58 L. ed. 115, 119, 120, 34 Sup. Ct. Rep. 20. The bankrupts undertook to 'forward' advice but only to 'provide' the drawee with funds."

The First National Bank's second contention was that it was, by subrogation, an equitable assignee of the bankrupt firm's account with the foreign bank to the amount of the draft it had issued and to which extent the bankrupt's account with the foreign bank had been debited. This argument was rejected by the Supreme Court. The Court said that the First National Bank might have bargained for a fund to be set apart for it in the foreign bank but it had not done so expressly and the general effect of the agreement was that it was merely bargaining for the obligation of Knauth, Nachod & Kuhne to have made available at the required time the necessary credit in the foreign bank. Said the Court (p. 366):

> "People dealing with large banks do not ordinarily seek the ambiguous security of an identified fund, they are satisfied if the bank gives them credit. We see no indications that the Trinidad bank was not perfectly content to know that it would have credit with the Banca Commerciale, and that in the usual course of things its drafts would be paid. Evidently with this conception of their duties the bankrupts asked the Italian bank 'to protect to the debit of our account the drafts' in question and others, and the branch bank to 'honor the above listed drafts.' . . .
>
> "The decision of this case depends more upon the general import of the transaction and upon what the parties were likely to want than upon the phrases that can be picked out from the several steps. We repeat that in our opinion what the parties meant to establish and what the respondent got was the assurance of a credit abroad to the extent of its check as in the case of a letter of credit, not an attenuated property right in an account to which no special funds were attached and the particulars of which neither the respondent nor the purchaser of the check could know."

The second part of the opinion of the Court in the Equitable Trust case is especially interesting. One of appellant's arguments is that it was an equitable assignee of the cash deposited in Franklin. The foregoing case shows that an equitable assignment can arise only where the depositor expressly stipulates for a fund to be set aside. In the present case the appellant did not so stipulate. Since it failed to do so, there is no fund upon which an equitable assignment can operate and, therefore, this theory can no more sustain it than any of the other three advanced by it in seeking a preference.

Blakey v. Brinson establishes that a deposit with a bank for a particular purpose does not create a trust where the depositor fails to stipulate that the funds are to be segregated, and *First National Bank v. Equitable Trust Co.* establishes that this is true even though the particular purpose involves making funds available to the depositor at a distant point.

Other cases to the same effect are:

Great Atlantic and Pacific Tea Company v. Citizens National Bank, 66 F. (2) 883 (C. C. A. 3d 1933);

Commercial National Bank v. Armstrong, 148 U. S. 50, 37 L. Ed. 363;

Keyes v. Paducah & I. R. Co., 61 F. (2d) 611, (C. C. A. 6th 1932);

Northern Sugar Corporation v. Thompson, 13 F. (2d) 829 (C. C. A. 8th 1926);

Santee Timber Corporation v. Elliott, 70 F. (2d) 179 (C. C. A. 4th 1934);

Kurecki v. Buck, 71 F. (2d) 227 (C. C. A. 7th 1934).

Of these cases the first two are important in that they likewise establish that the mere fact that the purpose for which the deposit is made is the transmission of funds from one point to another will not, without more, give rise to a fiduciary relationship rather than the usual debtor-creditor one; and they also establish that the mere fact that the funds deposited are to be held by the bank for a very short period of time will not, without more, give rise to any more than a debtor-creditor relationship. These cases are important because appellant in asserting a trust relationship in the present case relies chiefly on the fact that the funds deposited by it were to be transferred, and also that they were to be transferred very quickly.

Great Atlantic & Pacific Tea Company v. Citizens National Bank, 66 F. (2d) 883, C. C. A. 3 (1933), closely parallels the instant case. As did appellant, the Atlantic and Pacific Tea Company desired to have its funds transferred from its stores in different cities to the City of Pittsburgh. The tea company entered into an agreement with the bank whereby $2,000. was placed on deposit as an open dormant balance which was not to be disturbed without written notice. The agreement further provided (p. 883):

> "Deposits will be made daily by our representatives who will leave with you, two copies of the form showing the amount deposited. One of these forms should be verified by your Teller, or proper officer, and attached to your draft, which will be mailed the same day to the First National Bank at Pittsburgh. The other copy will be retained for your records. A tissue copy will remain in the Manager's book which you are requested to verify also. . . ."

It was customary for the managers of the company's stores to accompany their daily deposits in the bank with a ticket in the following form:

"Citizens' National Bank
(Name of Bank)
at
Andergrift, Pa.

accepts the amount listed below for immediate transfer to the First National Bank at Pittsburgh, Pa., for the account of The Great Atlantic & Pacific Tea Company in accordance with agreement in effect.

Currency	$254.00
Silver	36.00
Checks—List below	
	6.00
	23.44
	1.15
	12.25
Total	332.84"

In accordance with the agreement and without the objection of the tea company the bank remitted to the Pittsburgh bank the amount of the daily deposits by drawing drafts on one of its correspondents payable to the Pittsburgh bank for deposit to the credit of the tea company. After the close of the bank's business on Saturday, October 3rd, certain deposits were made which were never paid over to the tea company because the bank closed on October 5, 1931. The tea company brought suit against the Receiver of the bank contending that it was entitled to a preference in these deposits. The court held that no preference should be granted as no trust was created, the bank's obligation to transmit being purely contractual. Said the court (p. 884):

> "The agreement of the parties is, of course, for the transmission of the company's money from its stores to one of its central depositories. The agreement is not ambiguous. It contemplates daily deposits of the

company's funds in the bank and the transmission of the accumulated deposits of the day at the close of business to a distant bank. The method of transmitting the funds is by the bank's draft. Whenever the company made a deposit in the bank, the funds were mingled with the common mass of the bank's money, to be used as the bank would choose. There was no stipulation nor expectation that the deposits were to be set apart as a trust fund and held as such for the depositor; in other words, the company purchased the credit of the bank. There is no question but that is what the agreement means, for it says so in so many words, and the necessary conclusion is that the obligation of the bank here is purely contractual. In re A. Bolognesi & Company, 254 F. 770 (C. C. A. 2); Equitable Trust Company of N. Y., etc., v. First National Bank, etc., 275 U. S. 359, 48 S. Ct. 167, 72 L. Ed. 313; Stone, Some Legal Problems Involved in the Transmission of Funds, 21 Col. L. R. 507, 514."

The tea company also contended that there was a constructive trust in the deposit because the bank's officers knew at the time it accepted the deposit that the bank was insolvent. The court held that since at the time the deposits were accepted the bank was not hopelessly insolvent but actually had the honest hope of avoiding the inevitable, under the usual rule it was not guilty in taking the deposit and therefore no constructive trust arose.

The decision on this latter point is illuminating in the light of appellant's contention here in the last pages of its brief that the Franklin Trust Company was guilty of fraud in taking the deposits on October 2nd and 3rd as the bank's officers presumably knew it was insolvent. There is nothing in the record to show that the bank was insolvent on October 5, 1931, when it closed. The only allegation is that it

was taken into possession by the Secretary of Banking but no presumption of insolvency can be drawn from that fact alone as under the Banking Act of 1923 the Secretary of Banking may take possession of the business or property of a bank for any one of nine reasons, most of which do not involve insolvency. (See Appendix page 83.) Moreover, even if the bank were insolvent, there is nothing in the record to show that its officers knew that it was hopelessly insolvent or even that they knew that it was insolvent at all. Therefore there is nothing from which the court could infer that the bank in accepting the deposit was guilty of fraud upon the appellant.

In *Commercial National Bank v. Armstrong, supra,* the Commercial National Bank of Philadelphia (hereafter called "Commercial") brought suit against Armstrong as Receiver of the Fidelity National Bank of Cincinnati (hereafter called "Fidelity") alleging that he held certain moneys received as receiver in trust for Commercial. The Fidelity had entered into an agreement with the Commercial whereby Fidelity was to collect items for the Commercial "at par all points west of Pennsylvania and remit the 1st, 11th, and 21st of each month". The items sent to Fidelity under this agreement were endorsed for collection for the Commercial. On June 20, 1887, Fidelity failed, having in its hands or in the hands of other banks to which the same had been sent by it for collection proceeds of paper forwarded it by plaintiff amounting to $16,851.92. It was in these proceeds that Commercial claimed a preference. The Supreme Court held that while the Fidelity was the agent of Commercial before collection, it became the debtor after collection, but it held that collection did not occur for the purpose of changing the agency relationship to one of debtor-creditor unless and until Fidelity either received the

funds from its correspondent banks or what was equivalent to the receiving, had its indebtedness to its correspondent banks canceled by use of the proceeds prior to its failure. In holding that the Fidelity became a debtor of Commercial after collection, the court said that this was based upon the custom of banks to make use of the funds after collection in the absence of a stipulation to the contrary and the court felt that the fact that it had the use of the funds for only a very short time would not alter the rule. Said the court (p. 367):

> ". . . by the terms of the arrangement between the plaintiff and the Fidelity the relation of debtor and creditor was created when the collections were fully made. The agreement was to collect at par, and remit the first, eleventh and twenty-first of each month. Collections intermediate those dates were, by the custom of banks and the evident understanding of the parties, to be mingled with the general funds of the Fidelity and used in its business. *The fact that the intervals between the dates for remitting were brief is immaterial. The principle is the same as if the Fidelity was to remit only once every six months. It was the contemplation of the parties, and must be so adjudged according to the ordinary custom of banking, that these collections were not to be placed on special deposit and held until the day for remitting.* The very fact that collections were to be made at par shows that the compensation for the trouble and expense of collection was understood to be the temporary deposit of the funds thus collected and the temporary use thereof by the Fidelity. . . .
>
> ". . . Bearing in mind the custom of banks, it cannot be that the parties understood that the collections made by the Fidelity during the intervals between the days of remitting were to be made special deposits,

but on the contrary it is clear that they intended that the moneys thus received should pass into the general funds of the bank and be used by it as other funds, and that when the day for remitting came the remittance should be made out of such general funds." (Italics supplied.)

The following cases are also interesting in that they establish that a deposit of money for a particular purpose does not give rise to a trust relationship where the depositor fails to stipulate that the bank is not to have the use of the funds.

In *Keyes v. Paducah & I. R. Co.*, 61 F. (2d) 611 (C. C. A. 6th 1932), funds were deposited in the National Bank of Kentucky on an order of the court pending the outcome of litigation between a taxpayer and the county to determine whether certain taxes were due. A draft for $8000. was deposited by the railroad taxpayer for which a receipt was given by the bank. After the bank had collected the draft it advised the railroad's counsel as follows (p. 612):

"Acknowledging receipt of your letter of the 12th, beg to advise that the draft for Eight Thousand Dollars which you left with this bank for collection has been paid, and we are holding the proceeds in form of a cashier's check awaiting the time when your treasurer will, as you suggested in your letter, take the matter up with us.

"The court order accompanying your letter in the case of Paducah & Illinois Railroad Company, plaintiff, v. Holt, Sheriff, et al., defendant, has been filed for future reference."

Some months before the suit was ended the bank failed and thereafter when the court finally held that the railroad need not pay the tax in question the railroad brought suit

for full payment of the amount deposited. After a full discussion of general and special deposits the court held that the deposit in question was a general one and that the depositor was entitled to no preference. Said the court (p. 613):

> "Whether a deposit in a bank is general or special depends upon the mutual understanding, and intention of the parties at the time such deposit is made, and a deposit made in the ordinary course of business is presumed to be general, and the burden of proof is upon the depositor to overcome such presumption by proving that the deposit was made upon such terms and conditions as constituted a special deposit, or a deposit for a specific purpose, as distinguished from a general deposit. Northern Sugar Corp. v. Thompson (C. C. A.) 13 F. (2d) 829.
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> "Having in mind the nature of a special deposit, the trust relationship that results, and the initial presumption against its existence, it becomes necessary to determine what kind of a deposit was made in the instant case. If the deposit was special, its character must be derived from the terms of the court order directing it, the receipt given by the bank, and the bank's letter acknowledging payment of the draft. There is no other evidence. We fail to find in any of these instruments, herein sufficiently recited, any indication that it was the intention of the court or of the parties that the avails of the draft were to be segregated and kept as a separate fund until its disposition was directed by an order of the court. There was certainly no express direction in the order of the court to keep the funds deposited separate and distinct from the general funds of the bank, nor is any such direction to be clearly implied. That the parties did not themselves so interpret the arrangement seems equally clear. The bank's letter of June 15, 1929, informed the depositor

that the bank was holding the proceeds of the deposited draft in the form of a cashier's check. This could have but one meaning, and that is that the funds received were held as part of the general funds of the bank, and were represented by the bank's check upon itself, to be delivered to the successful litigant upon the order of the court. Although this letter was received by the depositor seventeen months before the determination of the litigation, and fifteen months before the bank failed, it does not appear that any protest was made to the bank's method of handling the fund, nor was a contrary understanding expressed by the depositor.

It would of course have been competent for the court, or for the parties, to have created a trust fund awaiting the outcome of the litigation. While there is no exclusive formula recognized by the law to accomplish such purpose, the inclusion of apt words of direction in the court order, in the instructions of the depositor to the bank, or in the form of receipt demanded, could very easily have brought it about. As was said by the Supreme Court in the recent case of Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 517, 76 L. Ed. 1089: 'It would have been equally competent for respondent to have provided for the purchase of the bonds either by the creation of a trust of funds in the hands of the bank, to be used for that purpose, or by establishing with it a credit to be debited with the cost of the bonds when purchased. But only if the former was the method adopted could respondent, upon the bank's insolvency and failure to purchase the bonds, recover the fund or its proceeds, if traceable, in preference to general creditors.' ''

In *Northern Sugar Corp. v. Thompson,* 13 F. (2d) 829 (C. C. A. 8th 1926), plaintiff, a sugar corporation, opened an account in the Wells National Bank for the purpose of making payment to farmers for beets purchased. Plaintiff

arranged to deposit with the bank a fund equal to the total amount of the payroll and would disburse the same by checks payable to the farmers, the checks to be lithographed with the words "Beet Payroll". When these particular funds were deposited, the bank was asked to place them to the credit of the "Beet Payroll Account." When the bank failed, there was some $29,000. in this account and the plaintiff sought to obtain a preference on the theory that the fund was held in trust. The court held that the plaintiff was entitled only to a depositor's status. Although the plaintiff had a particular purpose in mind in making the deposit, the court could find no agreement between the plaintiff and the bank that the funds

> "deposited to cover payroll checks should be held by the bank as a special fund, separate and apart from other general funds of the bank, or that they should be treated by the bank in any way different from a general deposit."

The Court said further (p. 832):

> "It is not an uncommon practice today for the large corporate organizations to carry several different accounts in the same bank. These accounts might be properly called departmental accounts. In such accounts funds are deposited, and checked out to pay the obligations of a particular department. Thus, in a sense, these deposits are made for the purpose of paying a particular class of obligations. But it is not the intention of the parties that the bank in accepting such deposits, shall act as the agent of the corporation, but such deposits are intended to be general deposits. The purpose of the corporation in carrying such separate accounts is not to reserve title to the deposits in itself, but to keep the transactions of its several departments separate from each other, and to facilitate the keeping of its books and records."

It has been shown that appellant agreed that Franklin Trust Company was not to segregate its deposits but was to mingle appellant's funds with its own and to perform its obligation to make funds available to appellant in New York City by using its (Franklin's) own funds or its credit with its New York correspondents. It follows from the cases cited above that no trust or fiduciary relationship existed between Franklin and appellant but only the usual debtor-creditor relationship and appellant therefore is entitled to no preference in the assets of Franklin Trust Company but must share pro rata with its general depositors.

(1) *Appellant's Four Theories as to the Creation of a Trust or Fiduciary Relationship Are Inapplicable to the Facts of This Case.*

Notwithstanding the authorities set forth above appellant argues that a fiduciary relationship existed between it and Franklin Trust Company with respect to the deposit in the Franklin and sets forth four legal theories upon which the assertion of fiduciary relationship might be based, with the consequent allowance of preference. Appellant's four theories are as follows:

> "(1) acceptance of money from one person for delivery to another constitutes the taker a trustee; (2) acceptance by a bank of a deposit for a particular purpose makes the bank a trustee; (3) acceptance by a bank from a customer of a deposit for the purpose of purchasing cash for the customer in another city constitutes the bank a trustee; and (4) equity regards as done that which ought to have been done."

In view of the fact that Franklin Trust Company had the right to use the funds in question, no fiduciary relation-

ship arose between it and appellant. Consequently not one of appellant's four theories and none of the authorities cited by it has any application to the facts of this case.

Appellant's first theory, that the "acceptance of money from one person for delivery to another constitutes the taker a trustee for the latter" is not in point.

1. No money was to be delivered from one person to another. The deposits in Philadelphia were made by appellant and the funds in New York were delivered to appellant.

2. As has been stated, a large part of the money to be delivered in New York consisted not of money received by Franklin Trust Company from appellant but of money actually derived from Franklin's own general funds as a result of money deposited in other banks by appellant, and for which Franklin received not cash but merely a credit on the other bank.

3. In any event, since the decision of the Supreme Court in *Equitable Trust Company v. First National Bank, supra,* a mere agreement by a bank to make funds available in another city as a result of a deposit made with it in one city does not give rise to any trust or fiduciary relationship unless the depositor stipulates that the deposit is to be segregated and maintained in identifiable condition. This theory contemplates relations between individuals and not relations with banks in the absence of a special agreement for segregation of the funds. For this reason, *McKee v. Lamon,* 159 U. S. 317 (1895), cited by appellant, is not in point, because no bank was involved, and therefore the presumption that the bank is to have the use of the funds deposited and furnish its general obligation

did not arise. The other cases under this section deal with escrow agreements and other situations having no relation to this case, and throwing no light upon it. Appellant's purpose in citing these cases seems to be to show that the custom of banks using funds deposited with them is not established as part of the agreement in this case, because not properly pleaded. This custom is so universal that a rule of law has been established that a bank of deposit has the right to use funds deposited with it and the burden is on the depositor to establish that the right to use the funds on the part of the bank was taken away by the agreement.

For its second legal proposition that "acceptance by a bank of deposits for a specific designated or particular purpose constitutes the bank a trustee thereof until the purpose is accomplished", appellant cites a wealth of authority. *Blakey v. Brinson, supra,* however, clearly establishes that irrespective of the purpose for which a deposit is made, a trust or fiduciary relationship does not arise between the bank and the depositor unless the depositor by agreement avoids the customary effect of a deposit, that is, that the depositor is merely a creditor and has the bank's general obligation to carry out the purpose for which the deposit is made. The burden is on the depositor to show that he had an understanding with the bank that the particular deposit was not to be used but was to be segregated to be used in specie for the purpose for which it was deposited.

The decision in *Blakey v. Brinson* confirms the rule as laid down in the Restatement of the Law of Trusts of the American Law Institute, which in Section 12, Comment (h) provides:

> "If money is deposited in a bank for a special purpose, the bank is a trustee or bailee of the money if, but

only if, it is the understanding of the parties that the money deposited is not to be used by the bank for its own purposes."

The authorities set forth earlier in appellee's brief at pages 51-68, are so clear that it would be profitless to dissect the eighteen cases cited by appellant on pages 43-53 of its brief. Most of them are not in point for obvious reasons. Thus in some of them (e. g., *Libby v. Hopkins,* 104 U. S. 303 (1881), and *Vosburgh's Estate,* 279 Pa. 329 (1924), the alleged fiduciary was not a bank, so that the presumption applicable to the present case, that a bank is to have a right to use the funds in the absence of an agreement to the contrary, was not involved. In other cases (e. g., *Merchants National Bank v. School District,* 94 F. 705, C. C. A. 9 (1899); *Smith v. Motley,* 150 F. 266, C. C. A. 6 (1906); *Girard Avenue Title and Trust Company Case,* 317 Pa. 313 (1935)) the facts gave rise to a trust *ex maleficio,* and they therefore have no application to this case. In certain other cases it was clear that the bank was to hold the funds as agent. And to the extent that any of such cases are used as general authority for the proposition that a deposit for a specific purpose, without more, gives rise to a fiduciary relationship, they must yield to the rule as established in *Blakey v. Brinson* and *Equitable Trust Company v. First National Bank,* that irrespective of the purpose, the only question to be answered in deciding whether or not a deposit gives rise to a fiduciary relationship is whether the depositor had a specific understanding with the bank that the depositor's funds were to be segregated until the purpose was accomplished. If the bank is to have the right to use the funds and furnish its obligation for the purpose, then no fiduciary relationship arises.

Appellant's third theory, that "acceptance by a bank from a customer of a deposit for the purpose of purchasing cash for the customer in another city, constitutes the bank a trustee", is not in point. Appellant was not purchasing cash but was merely acquiring Franklin Trust Company's obligation to have funds available to it in New York City. The language of Justice Stone in his article in Columbia Law Review, already quoted on pages 49-50, *supra,* is pertinent here.

The cases that appellant cites under this sub-heading are cases that might just as well have been put under its Subdivision (1) or (2). They involve the use of a bank by a depositor to make funds available to it at a distant point. Without discussing these cases in detail, appellee submits that the rule of *Equitable Trust Company v. First National Bank,* p. 56, *supra,* is clear that the mere agreement by a bank to make funds available to a depositor at another point does not give rise to a trust relationship where the bank has not agreed to set aside the fund deposited with it.

As to its fourth legal theory, appellant contends that—

> "Under the maxim, equity regards as done that which ought to have been done, there was an equitable assignment of the cash to petitioner."

This argument has already been disposed of by appellee in its discussion of *Equitable Trust Company v. First National Bank,* at pages 57-58 of this brief. It will suffice here to say that a transaction cannot give rise to an equitable assignment in favor of a depositor unless he can point to a specific fund which the bank has agreed to set aside. There was no such fund in this case, in view of the fact that Franklin Trust Company had the right to use

funds deposited with it, and merely gave its obligation to make funds available at the required times. In the two cases cited by appellant, *Early & Daniel Co. v. Pearson,* 36 F. (2d) 732 (C. C. A. 5th, 1929), and *Fourth Street Bank v. Yardley,* 165 U. S. 634, 41 L. ed. 855, 17 S. Ct. 439 (1897), there was a specific fund or credit which the bank had set aside for the benefit of the plaintiffs and to which they accordingly had the right to look when the bank failed.

In conclusion it is submitted that appellant's four theories can be combined into one theory, namely, that a deposit designated to be special and in trust and not to be used by the bank of deposit can be claimed in full upon insolvency of the bank. If appellant could establish such an agreement with the Franklin Trust Company with regard to its deposit it might succeed on some one or more of the four theories it advanced and it would seem immaterial which one the Court selected. Appellant, however, has not proved that the deposit made was to be in trust; rather the agreement shows that the usual custom was to prevail and that the bank was to have the use of the funds and furnish only its general obligation to make payments at the time and place specified. Since that is the case, appellant is in no better position than any other depositor and must share pro rata with other claimants of the same class.

(*b*) *Appellant Is Entitled to No Preference in the Proceeds of Drafts and Checks Deposited With Franklin Trust Company and Collected After It Was Taken Over by Appellee.*

Apart from any question of establishing a trust in the deposits, appellant contends that it is entitled to a prefer-

ence in certain checks and drafts amounting to $8,747.66, which had not been collected at the time Franklin closed on October 5, 1931. This contention is made under the *Pennsylvania Bank Collection Act of June 13, 1931,* P. L. 568, which for certain purposes makes the bank of deposit and other collecting banks the agent of a depositor of commercial paper.

Under the federal rule, title to checks and drafts indorsed without restriction passes to the bank of deposit at the time of deposit, and the depositor thereafter becomes a creditor of the bank, even prior to collection. *City of Douglas v. Federal Reserve Bank,* 271 U. S. 489; 70 L. Ed. 1051. There is nothing in the record to show that these checks were indorsed restrictively, and, apart from the Pennsylvania statute above-mentioned, appellant has failed to show that the federal rule would not be applicable to the deposits of checks and drafts made by it.

It may be conceded that to the extent the foregoing statute is applicable, the federal rule must yield to it. It is appellee's contention, however, that by its terms that statute is not applicable to this case. For it provides in Section 2 that "*except as otherwise provided by agreement* . . . the bank of deposit shall be agent of the depositor for its collection . . ." (Italics supplied.) The effect of the agreement entered into in 1925, between Franklin Trust Company and appellant, long before this Bank Collection Act was enacted, was to place the deposit of checks and drafts in the same category as the deposits of cash so that immediately upon deposit appellant acquired a general claim against Franklin Trust Company by reason of the deposit. Appellant's bill of complaint recites that one subdivision of the agreement was that (R. pp. 31-32):

"(c) The Franklin Trust Company would accept from your orator's distributors in Philadelphia, cash, also drafts and checks for collection, for the purpose of forwarding the cash, together with the proceeds of the drafts and checks, on Monday of each week to your orator, or its depository, in New York City; said account to be known as a 'Deposit Account'."

This averment does indicate that the deposit of drafts and checks was differentiated from the deposit of cash as it speaks of the drafts and checks being accepted "for collection". As pointed out in appellee's counter-statement of the case, however, this particular averment cannot be divorced from the corresponding averment in appellee's answer. This answer does not admit that the drafts and checks were accepted for collection. Rather, it shows that checks, drafts and cash were all received to make one deposit account. Appellee's averment on this point reads as follows (R. p. 48):

(c) "As by reference to the exhibits to the amended Bill of Complaint, as amended, will more specifically appear, your deponents aver that General Baking Company, the complainant, agreed to open a 'deposit account' in the Franklin Trust Company, wherein all moneys (including checks, cash and drafts) received by the three Philadelphia plants of the complainant were to be deposited, said deposits to be credited to the complainant, advices of each deposit to be forwarded to the offices of the General Baking Company in New York, and on Monday of each week the balance in the deposit account (as augmented by the funds received under the terms and conditions hereinafter set forth) to be forwarded by the Franklin Trust Company to the General Baking Company in New York or its depository."

Appellee's qualification of appellant's averment on this point is based upon the exhibits attached to appellant's bill. The oral agreement of August 25, 1925, was merely a consummation of the negotiations between the parties, as shown by these Exhibits A, B and C. (R. pp. 39-42.) An examination of these exhibits shows that at no point did either Franklin or appellant consider the deposit of checks and drafts in any different light from the deposit of cash. In speaking of this deposit account, both appellant and Franklin Trust Company speak only of the "moneys" to be deposited to appellant's credit in the deposit account. It is submitted that the use of this word "moneys" establishes that the deposits made by appellant were to go to its general credit immediately and that this was true whether the deposits were checks, drafts or cash. This was the view taken by Judge Kirkpatrick, of the District Court, who said in his opinion (R. p. 24):

> "Even if the averment of the bill that the deposits were received 'for collection' in the ordinary commercial sense could be taken as admitted (which is doubtful in view of the qualified answer) it would make little difference, since it is conceded that cash, drafts and checks were all to go into the deposit account indiscriminately under the same terms and of course it would be patently absurd to speak of accepting cash deposit for collection."

Appellee therefore respectfully submits that appellant has failed to establish that the uncollected checks and drafts were deposited for collection within the meaning of the provisions of the Pennsylvania Bank Collection Act and that both the District Court and the Circuit Court of Appeals correctly held that appellant was entitled to no preference in their proceeds.

(c) *Appellant Is Entitled to No Preference in the Cash, Checks and Drafts Deposited in the Correspondent Banks and Received by Appellee After the Franklin Trust Company Closed.*

Apart from any question of establishing a trust, appellant asserts a preference in the cash, drafts and checks in the amount of $32,403.26, which had been deposited with the correspondent banks of Franklin pursuant to the agreement of August 25, 1925. Appellant bases this claim for preference on the fact that Franklin Trust Company had not received any notice of these deposits prior to its closing and the further fact that the funds deposited never came into the possession of Franklin but were received by appellee to be put into escrow pending the outcome of this litigation.

The fact that Franklin Trust Company had not received notice of the deposits made in its correspondent banks prior to collection, and never actually received the funds deposited, is immaterial. Appellee has shown earlier in this brief that no trust relationship existed between Franklin Trust Company and appellant as to deposits made in correspondent banks, any more than it did as to deposits made in Franklin Trust Company itself. The effect of all the deposits was to create a debtor-creditor relationship between Franklin Trust Company and appellant, and this relationship arose immediately upon deposit. That the deposits in correspondent banks immediately became Franklin's general obligation is shown by the fact that such deposits were credited to Franklin's account in those banks and subject to Franklin's check only, and that Franklin undertook to make these amounts good to appellant in New York City. The effect of the agreement was to make a deposit in a correspondent bank actually and im-

mediately equivalent to a deposit in Franklin Trust Company. It is true that Franklin forwarded funds equivalent to these deposits in correspondent banks only after it had received advices of the same from those banks, but the purpose of the advices was not to give rise to Franklin's obligation but merely to inform it as to its extent at any given time. By the agreement Franklin was bound to use its funds to produce in New York the equivalent of deposits made in the correspondent banks, but it had to receive the advices in order to know exactly what amount it was to send. Consequently since Franklin's obligation arose as soon as the deposit was made, the fact that it never received the funds nor received notice of the deposits is immaterial. The obligation, not the possession, is the important thing, and since appellant was entitled to and received Franklin's obligation immediately for these deposits, it is entitled to no preference in them.

The sole authority relied upon by appellant for its claim to a preference in these deposits in the correspondent banks is *Commercial Bank of Pennsylvania v. Armstrong*, 148 U. S. 50, 37 L. Ed. 363 (1893). That case is not in point. There the Fidelity Bank in Cleveland agreed to collect commercial paper in the west for the Commercial Bank of Pennsylvania, located in Philadelphia, and to remit "on the 1st, 11th and 21st of each month". The paper forwarded for collection was stamped: "Pay Fidelity National Bank of Cincinnati, O., or order, for collection for Commercial Bank of Philadelphia, Pa., E. P. Graham, cashier." In commenting on the agreement this Court said (p. 56): "The Fidelity received the paper as agent, and the indorsement 'for collection' was notice that its possession was that of agent and not of owner." In setting forth this case, appellant states that these collections were to be

made "in consideration of the temporary use of the funds". As a matter of fact, there was no express agreement between the banks that Fidelity was to have the use of the funds any more than there was in the present case. The only agreement the Court had to construe was the agreement to collect and remit. While some of the commercial paper was in the process of collection, the Fidelity Bank failed and Commercial Bank asserted a preference in the proceeds of these collections. These proceeds at the time of Fidelity's failure were in the hands of sub-agent banks to which Fidelity had forwarded them for collection. In determining whether and to what extent the Commercial Bank should obtain a preference in these proceeds, the Court used two legal premises. First, it said that the effect of the agreement was to make Fidelity an agent of Commercial before collection, and, by custom, a debtor of Commercial after collection. The Court then went on to decide just when such commercial paper was collected, and it held that in those instances where the proceeds collected by the sub-agent banks had been used by them to cancel indebtedness of Fidelity Bank to them, Fidelity had collected and thereupon became a debtor of Commercial and the latter was entitled to no preference. In those instances, however, in which the proceeds were still in other collecting banks and had neither been forwarded to Fidelity nor used to cancel an indebtedness of Fidelity, the Court held such paper had not been collected, even though a notice had been sent to Fidelity of such collection, that the agency relationship between Fidelity and Commercial still existed, and that therefore Commercial was entitled to a preference in such proceeds.

That case is not in point here, because all it decided and all it purported to decide was at what point an agency relationship which admittedly existed between two banks

was transformed into a debtor-creditor relationship between those banks. Such a decision has no bearing on a case like the instant one, in which no agency or fiduciary relationship ever existed between Franklin Trust Company and appellant, but which amounted to a debtor-creditor relationship from the start. There is no evidence on the present record that checks were deposited in the correspondent banks "for collection" and as pointed out by Judge Kirkpatrick in his opinion in the lower court (R. p. 24): "It would be patently absurd to speak of accepting cash deposit for collection." Accordingly no agency relationship ever arose, either as to the cash or checks deposited in the correspondent banks. The parties having agreed that the relationship between Franklin Trust Company and appellant was, as to these deposits in correspondent banks, to be a debtor-creditor relationship immediately, questions as to when notice was received by Franklin from these banks, or when funds were transmitted from these banks, are immaterial, and a decision like *Commercial Bank v. Armstrong*, which uses these criteria in determining when a transition from an agency relationship into a debtor-creditor relationship occurs, has no bearing on our problem. Moreover the deposits in the correspondent banks were made to the credit of Franklin and were subject to its check alone. By the act of deposit appellant lost all interest in the funds as such and accepted in lieu thereof the general obligation of Franklin to pay appellant in New York in cash funds the following Monday the total amount of the deposits in Franklin and the correspondent banks. It is therefore submitted that appellant has failed to establish its claim to a preference in the deposits of $32,403.26 made by it to the credit of Franklin Trust Company in the correspondent banks and that the District Court and Circuit Court of Appeals properly so ruled.

(*d*) *Summary of Argument on the Merits.*

The District Court and the Circuit Court of Appeals both correctly held that appellant was entitled to no preference with respect to the deposits made by it in the Franklin Trust Company and the correspondent banks, and properly dismissed appellant's bill on the merits. Appellant is entitled to no preference as to the $40,842.51 of cash deposited in the Franklin Trust Company, in the $8,747.66 checks and drafts deposited in Franklin Trust Company, nor in the $32,403.26 total of cash, checks and drafts deposited in the correspondent banks of Franklin Trust Company, because the agreement between Franklin Trust Company and appellant was such that the deposits both of checks and cash gave title thereto to Franklin and gave rise to a debtor-creditor relationship and not to a trust relationship between Franklin Trust Company and appellant, and gave rise to such debtor-creditor relationship immediately upon deposit.

It is therefore submitted that the decree of the Circuit Court of Appeals for the Third Circuit entered on June 14, 1933, directing the District Court for the Eastern District of Pennsylvania to dismiss appellant's bill should be affirmed.

Respectfully submitted,

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Appendix.

THE RELEVANT SECTION OF THE PENNSYLVANIA BANKING ACT OF 1923, JUNE 15, P. L. 809, AS AMENDED BY ACT OF 1927, MAY 5, P. L. 762.

§ 19. Jurisdiction of courts

Whenever it shall become the right or duty of the Attorney General to proceed against any corporation or person under the supervision of the department, pursuant to the provisions of this act, he may, in his discretion, proceed either in the court of common pleas of Dauphin County or in the court of common pleas of the county where the banking house or other place of business of such corporation or person is located. (1923, June 15, P. L. 809, § 19.)

§ 21. Power of secretary to take possession

The secretary may, after hearing had upon notice given, with the approval and consent of the Attorney General, take possession of the business and property of any corporation or person subject to the supervision of the department, whenever it shall appear to him that such corporation or person:

I. Has violated any law regulating its or his business, and has persisted in such violation in disregard of an order duly made by the secretary;

II. Is conducting business in an unauthorized or unsafe manner and has persisted in disregard of an order duly made by the secretary;

III. Is in an unsafe or unsound condition to continue business: Provided, in such case, That the secretary may forthwith, without such hearing and consent of the Attorney General, take possession of the business and property of any such corporation or person receiving moneys on deposit, when and if, in his opinion the protection of depositors and the public requires such peremptory action;

IV. Has an impairment of capital, which has not been restored or made good within the time fixed by order of the secretary;

V. Has suspended payment of obligations;

VI. Has neglected or refused to comply with the terms of any lawfully issued order of the secretary;

VII. Has refused, upon proper demand, to submit the records and affairs of the business to the secretary, a deputy, or any duly authorized examiner or agent of the department;

VIII. Has refused to be examined upon oath or affirmation, regarding such affairs;

IX. Is in the hands of a receiver appointed by any court, or in any bankruptcy proceeding, or of an assignee or trustee for creditors appointed by such corporation or person.

The secretary may, in like manner, take possession of the business and property of any private or unincorporated bank, or the estate of any private banker, otherwise exempt from the supervision of the department, whenever such private or unincorporated bank shall have made an assignment for the benefit of creditors, or for any of the causes mentioned hereinbefore in this section. (1923, June 15, P. L. 809, § 21; 1927, May 5, P. L. 762, § 7.)

§ 22. Certificate of taking possession

When the secretary shall have duly taken possession of the business and property of a corporation or person as provided in section twenty-one of this act,[1] he shall forthwith make, under his hand and official seal, a certificate setting forth that he has so taken possession, and shall file such certificate in his office, and cause a certified copy thereof to be filed in the office of the prothonotary, who

[1] Section 21 of this title, ante.

shall index the same in the judgment index under the name of the corporation or person as defendant and the name of the secretary as plaintiff.

From and after the filing of such certified copy in the office of the prothonotary, the secretary shall supersede any receiver previously appointed by any court for, or any assignee or trustee for creditors appointed by, such corporation or person.

Such superseded receiver, assignee, or trustee shall forthwith file his account in the court having jurisdiction thereof, and pay over and deliver to the secretary all moneys, securities, assets, and property of such corporation or person in his custody, possession, or control. Said court shall allow credit for expenses and for the disbursements properly incurred or made prior to the taking possession by the secretary, and shall allow proper compensation to said receiver, assignee, or trustee, and his counsel, which, when determined, shall be paid out of the funds of said corporation or person in the hands of the secretary. (1923, June 15, P. L. 809, § 22.)

§ 23. Injunction to restrain secretary

Whenever the secretary takes possession of the property and business of any corporation or person, such corporation or person may, at any time within ten days, apply to the court for an order requiring the secretary to show cause why he should not be enjoined from continuing such possession. The secretary may be served personally wherever found within the State, or by leaving a copy with the deputy in charge of his office, or by serving the special deputy appointed by him in such proceeding. At the hearing, a copy, certified by the secretary or one of his deputies, of any report of a duly instituted examination of such corporation or person shall be prima facie evidence of the facts therein stated; and if, from such report or reports or other evidence, there shall appear to be just cause for the taking and continuing of possession by the secretary, he shall not be enjoined, unless such report or reports or other evidence

shall be overcome by proper proof produced by such corporation or person, in which event the court shall direct the secretary to refrain from further proceedings and to surrender such possession. (1923, June 15, P. L. 809, § 23; 1927, May 5, P. L. 762, § 8.)

§ 25. Notice to parties holding assets

When the secretary shall have taken possession of the property and business of any such corporation or person, he shall forthwith give notice in writing of such fact to all corporations and persons holding any assets thereof. No one having such notice or actual knowledge that the secretary has so taken possession shall have a lien or charge against any of the assets of such corporation or person for any charge, payment, advance, or clearance thereafter made or liability thereafter incurred. The status of all parties shall become fixed on the date the secretary files his certificates of possession in his office in Harrisburg, as provided in section twenty-two of this act.[1] (1923, June 15, P. L. 809, § 25; 1927, May 5, P. L. 762, § 9.)

§ 26. Inventory of assets

After the secretary has taken possession as aforesaid, he shall make, or cause to be made, a complete inventory of the assets of such corporation or person, which inventory shall be verified by oath or affirmation of the person or persons making the same, and shall forthwith file such inventory in his office. (1923, June 15, P. L. 809, § 26.)

§ 27. Suspension or continuation of business

The secretary is authorized, upon taking possession of the property and business of such corporation or person, to continue or suspend the business for such period as he may deem necessary to enable him to determine whether to liquidate the affairs of such corporation or person, and, during such period, to take such action as in his judgment is necessary to conserve the assets and business. (1923, June 15, P. L. 809, § 27.)

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[1] Section 22 of this title, ante.

§ 28. Surrender of possession by secretary

The secretary may, upon conditions approved by him, surrender possession for the purpose of permitting such corporation or person to resume business to sell or convey its or his property and franchise, or to merge or consolidate its or his business with that of another corporation or person in accordance with the laws of this Commonwealth, or because he is without funds to continue or liquidate the business and property of which he has taken possession; but he shall not authorize any decrease of capital stock by a corporation except upon compliance by the corporation with the provisions of law as to such decrease.

Whenever the secretary shall surrender possession under the provisions of this section, he shall forthwith issue an order, under his official seal, authorizing such corporation or person to resume business, to sell or convey its or his property and franchises, or to merge or consolidate as aforesaid, and shall file said order in his office, and cause a certified copy thereof to be filed in the office of the prothonotary, who shall thereupon cause the entries upon the judgment index made pursuant to section twenty-two of his act [1] to be satisfied. (1923, June 15, P. L. 809, § 28; 1927, May 5, P. L. 762, § 10.)

§ 29. Status and powers of secretary as receiver

Except as herein otherwise provided, the secretary shall, when he has taken possession of the business and property of a corporation or person, have all the rights, powers, and duties of a receiver appointed by any court of equity in this Commonwealth; and he shall be vested, in his official capacity, with all the rights, powers, and duties of such corporation or person and with all the property of such corporation or person, including debts due, liens, or securities therefor, and rights of action or redemption, whether or not the property of such corporation or person,

[1] Section 22 of this title, ante.

including debts due, liens, or securities therefor, and rights of action or redemption, are held in the name of such corporation or person, or in the name of some other corporation or person, but actually the property of the corporation or person of which, or of whom, the secretary has possession.

He shall be the representative of the creditors of the corporation or person, and entitled, as such, to have vacated and set aside, for the benefit of the creditors, any judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance, which could have been avoided by the creditors or any of them, or by which it is attempted to give any creditor unlawful preference over another.

He may, with leave of court obtained on petition after notice to all creditors of whom he has knowledge, surrender to the corporation or person any assets, including choses in action, whether the subject of pending proceedings or not, which are burdensome and of no advantage to creditors. (1923, June 15; P. L. 809, § 29; 1927, May 5, P. L. 762, § 11.)

§ 30. Power of court to make and enforce orders

The court having jurisdiction shall have power to make and enforce any and all orders necessary and appropriate to enable the secretary to discharge his duties in connection with the business, property, and affairs of any corporation or person taken into possession by the secretary under the provisions of this act, upon petition of the secretary, acting personally or through his duly authorized deputy, setting forth the facts; and the court shall also have the power, upon petition of the secretary, acting personally or through his duly authorized deputy, to order and direct other corporations or persons in possession of assets or property, belonging to the corporation or person in possession of the secretary, to transfer or convey said property or assets to the secretary, and to execute and deliver any and all necessary instruments in writing to accomplish that purpose. (1923, June 15, P. L. 809, § 30; 1927, May 5, P. L. 762, § 12.)

§ 31. Continuance of possession; exceptions

When the secretary shall have duly taken possession of the business and property of corporation or person as provided in section twenty-one of this act,[1] he shall hold such possession until the affairs of such corporation or person have been liquidated by him, unless:

I. He shall have been directed by order of court to surrender such possession pursuant to the provisions of section twenty-three of this act; [2]

II. He shall have permitted a resumption of business, or a sale or conveyance of property and franchises, or a merger or consolidation, pursuant to the provisions of section twenty-eight of this act; [3]

III. The stockholders of such corporation, after payment of all creditors in full, shall have elected a trustee or trustees, to continue the liquidation of such corporation, or the court shall have appointed such trustee or trustees, pursuant to the provisions of section fifty of this act,[4] and such trustee or trustees shall have duly qualified to take possession of the remaining assets of such corporation; or,

IV. The depositors and other creditors of such person and the expenses of such liquidation shall have been paid in full. (1923, June 15, P. L. 809, § 31.)

§ 34. Compromises

The secretary may, with leave of court, compound or compromise any debt, claim, or judgment due to the corporation or person, and discontinue any action or other proceeding pending therefor; if done in good faith and after proper inquiry; and may require all mortgages, conditional contracts, pledges, and liens of or upon any real or personal

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[1] Section 21 of this title, ante.
[2] Section 23 of this title, ante.
[3] Section 28 of this title, ante.
[4] Section 50 of this title, post.

property of such corporation or person, to be satisfied, canceled, or assigned to him, as he may deem best, or he may sell the property subject thereto. (1923, June 15, P. L. 809, § 34; 1927, May 5, P. L. 762, § 15.)

§ 35. Actions and suits

For the purpose of executing any of the powers and performing any of the duties hereby conferred and imposed upon him, the secretary may, in the name of the corporation or person, prosecute and defend any and all actions and proceedings at law, in equity, or otherwise, pending at the time when the secretary takes possession of the business and property of such corporation or person.

He may, by bill of discovery or other legal or equitable proceeding, obtain information of, and sue for and recover, any assets, debts, or damages, which such corporation or person might sue for and recover, or which any of the creditors might make available for the payment of their claims.

He may, at any time while he is in possession of the property and business of a corporation, institute and maintain against the directors, trustees, managers, or officers, any action or proceeding which is vested in such corporation or in the stockholders or creditors thereof.

He shall be liable to suit, in his representative capacity, by any person seeking to recover specific property, if such property could have been recovered as against the creditors of the corporation or person levying an execution thereon. (1923, June 15, P. L. 809, § 35.)

§ 36. Judgments not to be liens; stay of execution

No mechanic's lien shall attach, nor shall any other lien attach, to any of the property or assets of the corporation or person by reason of the entry of any judgment against such corporation or person after the secretary has taken possession of its or his property and business and filed a certificate in his office in the capitol at Harrisburg, as re-

quired by section twenty-two of this act,[1] and so long as such possession continues.

During such time, no execution or attachment shall issue against such corporation or person, nor shall any pending execution or attachment be proceeded with except by special leave of the court. (1923, June 15, P. L. 809, § 36; 1927, May 5, P. L. 762, § 16.)

§ 38. Inventory and appraisement; statement of liabilities

When the secretary has determined to liquidate the affairs of any such corporation or person, he shall forthwith cause an inventory and appraisement of the assets of such corporation or person, under oath or affirmation, to be made in duplicate, by two disinterested appraisers chosen by him, and shall file such inventories and appraisements, one in his office, and the other in the office of the prothonotary; and, for the purpose of enabling the secretary to do so, he or his duly authorized deputy is hereby empowered to call before him, by subpœna, with or without books and papers, and to examine, the corporation or person, or the officer, director, or employés thereof, taken in possession, under oath, or any person who, he or they have reason to believe, has knowledge of other or further assets of the said corporation or person, or any person who, he or they believe, can give information touching the same. Every witness shall be entitled to receive, out of the estate of the corporation or person, the usual witness fee and mileage for this attendance for these purposes. (1923, June 15, P. L. 809, § 38; 1927, May 5, P. L. 762, § 17.)

§ 41. Notice to depositors and creditors

When the secretary shall have determined to liquidate the affairs of such corporation or person, he shall forthwith give written or printed notice to all depositors to produce to him their deposit or pass books for settlement, stating in

[1] Section 22 of this title, ante.

such notice the amount which the books of the corporation or person show to be due to each depositor, subject to outstanding checks, and notifying such depositors that unless a settlement of the deposit or pass books shall show a different amount to be due, or unless a depositor shall, within four months from the date of such notice, make proof, in the matter hereinafter set forth, that the amount due him differs from the amount as shown by the books of the corporation or person, the amount last mentioned will be conclusive as to the amount of the claim of such depositor, subject, as aforesaid, to any outstanding checks.

The secretary shall, at the same time, give written or printed notice to all creditors other than depositors, so far as known to him, to make proof of their claims in the manner hereinafter set forth, within four months from the date of such notice, or be debarred from coming in upon the fund.

He shall also advertise such notices to depositors and other creditors in a newspaper, and in the legal newspaper, if any, designated by rules of court for publication of legal notices in said county, once a week for four successive weeks. (1923, June 15, P. L. 809, § 41.)

§ 42. Proof of claims of creditors

No claim other than the claim of a depositor shall be allowed unless the claimant, or someone for him if he cannot do so, shall, within four months from the date of such notice, furnish to the secretary a statement of his claim, together with a copy of any book entries pertaining thereto, or any note or other writing evidencing the same, verified by an affidavit in substantially the following form:

"I, (name of claimant) do solemnly swear (or affirm) that the above is a true statement of my claim against (name of corporation or person); that there are no credits or allowances against the same except as therein set forth; that I have not directly or indirectly made or entered into any bargain, arrangement, or agreement, express or im-

plied, to take or receive, directly or indirectly, any money, property, or consideration whatever, to or for myself, or to or for any other person, firm, or corporation whatever, other than my dividend as a creditor; and that there is no collateral security for said indebtedness, or any part thereof, held by me or anyone else other than as above set forth."

In case the claimant shall be a partnership or corporation, such affidavit shall be made by a member of the partnership, or by the treasurer or assistant treasurer of the corporation claimant, and the form thereof shall be modified accordingly.

The provisions of this section shall not apply to the claim of cestuis que trust or others to or against trust funds or property in the custody, possession, or control of a corporation or person, possession of whose business and property is taken by the secretary under the provisions of this act. (1923, June 15, P. L. 809, § 42; 1927, May 5, P. L. 762, § 18.)

§ 45. Partial or final account; objections

At the expiration of the time fixed by the notice and advertisement for the presentation of claims prescribed in section forty-one of this act,[1] the secretary may file a partial or final account, consisting of a statement of receipts and expenditures, together with a list of the claims which have been allowed, and, separately, a list of the claims which have been objected to or are disputed, showing, as to all claimants, the names, addresses, and amounts.

If no account is filed within a year from the time when the secretary takes possession, any party interested may petition the court for an order on the secretary requiring the filing of an account.

Any account filed by the secretary shall be duly verified by him under oath or affirmation. Upon the filing thereof, he shall give written or printed notice, to all the depositors

[1] Section 41 of this title, ante.

and other creditors known to him, of such filing, and that, unless objections shall be filed within thirty days from the date thereof, the same will be confirmed absolutely. He shall also, at the same time, advertise such notice in two newspapers once a week for four successive weeks.

During such period of thirty days, any depositor, other creditor, stockholder, or anyone having any interest, may file in the court objections in writing to said account or to the allowance of any of said claims, a copy of which objections shall forthwith be served upon the claimant whose claim is objected to, or his counsel, and upon the secretary, or his counsel, or the special deputy appointed by him in such proceeding. (1923, June 15, P. L. 809, § 45.)

§ 46. Distribution

If at the expiration of said period of thirty days from the filing of the account, no objections shall have been filed thereto, the same shall be confirmed absolutely. In case objections or exceptions are filed to any claim or claims, the account shall be confirmed absolutely as to those claims against which no objections or exceptions have been filed, and a partial or final dividend, as the case may be, shall be declared and paid by the secretary on all claims as to which no objections or exceptions have been filed. In case there shall be any disputed claim or any claim to which objections shall have been duly filed, the dividend shall be calculated as if all claims were valid and approved, and, after deducting and setting apart such portion of the dividend as may be declared on claims, in accordance with the priorities fixed by law, which are disputed or objected to, the balance shall be distributed among the other claims. If all or any of the claims disputed or objected to shall thereafter be determined to be valid, they shall then receive their portions of such dividend in accordance with the priorities fixed by law. If all or any of such claims be determined to be invalid, the portions of such dividend set apart for them

shall be distributed to the valid claims. (1923, June 15, P. L. 809, § 46; 1927, May 5, P. L. 762, § 20.)

§ 47. Conclusiveness of confirmation and distribution; records; final destruction

The confirmation of a partial account and distribution thereunder, as aforesaid, shall be conclusive only as to the fund distributed, and shall not prevent the proof and allowance, out of the fund involved in any subsequent account, of claims not presented in time for allowance out of such previous fund.

The confirmation of a final account and distribution thereunder, after the objections thereto, if any, have been adjudicated as hereinafter provided, shall be conclusive; and shall work and effect a discharge of the secretary and all deputies or their sureties, from all liability in the matter; and the secretary or his successor, except as hereinafter provided in section fifty of this act,[1] is authorized and empowered to destroy all records belonging to the corporation or person in his possession at the expiration of seven years from the date of the absolute confirmation of the final account of the secretary. (1923, June 15, P. L. 809, § 47; 1927, May 5, P. L. 762, § 21.)

§ 48. Hearing and decision of matters in controversy

If there shall be claims disputed or objected to, or if there shall be objection to the account, the court shall itself, without delay, hear and decide the matters in controversy. The court shall fix a time and place for the hearing, of which notice shall be given by the secretary to all depositors and other creditors whose claims have been disallowed by the secretary, or excepted or objected to by other depositors, creditors, or stockholders, as well as to those depositors, creditors, or stockholders, who have objected to the account or to claims allowed in the account. Said notice

[1] Section 50 of this title, post.

shall also set forth that all parties whose claims are disputed or objected to must appear at said time and place and prove their claims or be debarred from coming in upon the fund for distribution. (1923, June 15, P. L. 809, § 48; 1927, May 5, P. L. 762, § 22.)

§ 49. Expenses to be paid out of fund

All assessments, charges, and penalties due to the department by such corporation or person, all expenses of the taking and maintaining possession of the business and property or the continuing of the business by the secretary, and all expenses of liquidation under the provisions of this act, shall first be payable out of the funds of such corporation or person, including the compensation of special deputies, assistants, and others employed by the secretary to assist him in such proceedings; the allowance of all such expenses to be subject to the approval of the court. (1923, June 15, P. L. 809, § 49.)

§ 50. Distribution of balance; liquidating trustees

If, after the filing and confirmation of the final account of the secretary, and the payment of all creditors in full, and the return to stockholders, who have paid to the secretary the amounts demanded pursuant to section thirty-seven of this act,[1] of their pro rata shares of any such amounts not necessary to pay creditors in full, there shall remain a balance in the hands of the secretary, he shall call a meeting of the stockholders by serving written or printed notice upon them at least thirty days before the day fixed for the meeting.

At such meeting, the stockholders shall elect by ballot a trustee or trustees for the purpose of completing the liquidation. A majority of the stock present in person or by proxy shall be necessary to elect. Should the stockholders fail or refuse to elect, the secretary or any stockholder may

[1] Section 37 of this title, ante.

petition the court for the appointment of such trustee or trustees, who, when appointed, shall give bond to the Commonwealth in such amount, with such surety, and on such conditions, as the court may direct.

When such trustee or trustees have been duly elected or appointed as aforesaid, the secretary shall then transfer, convey, and deliver to such trustee or trustees all the assets of the corporation then remaining in his hands. He shall thereupon be discharged from all further liability to such corporation and its creditors, and shall file a certified copy of the proceedings of such stockholders' meeting in his office, and cause a certified copy thereof to be filed in the office of the prothonotary. No powers subject to the supervision of the department shall thereafter be exercised by such corporation, except by permission of the secretary, and after compliance by such corporation with all the requirements of law as to a new corporation desiring to exercise such powers. (1923, June 15, P. L. 809, § 50.)